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NOS. 22489 and 22489A

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

FRIEND AND COMPANY, a corporation,
and WILBER H. FRIEND,

Defendants-Appellants,

vs.

H. A. FRIEND AND COMPANY, INC.,

Plaintiff-Appellee.

BRIEF ON BEHALF OF APPELLANTS FRIEND AND COMPANY AND WILBER H. FRIEND

APPEAL FROM
THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

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STATEMENT OF THE PLEADINGS AND JURISDICTION

The two Appeals Nos. 22489 and 22489A correspond with Civil Actions Nos. 64-850-WPG and 66-470-WPG, respectively, filed in the United States District Court for the Central District of California, and consolidated for trial. The first of these actions (Appeal No. 22489) was commenced on June 17, 1964 by plaintiff-appellee filing its Complaint (Ct 2) 1/ alleging

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1/ In this brief the following reference terminology is used: Ct for pages of the Clerk's Transcript; Rt for pages of the Reporter's Transcript of trial proceedings; Exh. for trial exhibits, the plaintiff's exhibits being identified by numbers, the defendants' exhibits by letters; Adm. for Admission; Int. Ans. for Interrogatory Answer.

jurisdiction under the provisions of the Federal Trademark Law of 1946 (15 U.S.C. 1050), and upon the ground of diversity of citizenship between plaintiff and defendants wherein the amount in controversy was alleged to exceed the sum of $10,000, exclusive of interest and costs. The said Complaint was set up in six causes of action, the first four of which were for trademark infringement and unfair competition based on allegations of infringement of alleged trademarks "Friends" and a registration for it, No. 655,848, issued December 17, 1957 (Exh. 1); and "Barrister Bond" and "Banner". The said original complaint did not allege any registrations for either "Banner" or "Barrister Bond", as there has never been a registration for "Banner", and the registration for "Barrister Bond" No. 274,875, issued September 9, 1930 (Exh. 2) was at all times involved in this suit up to the commencement thereof, owned by Gilbert Paper Company. The Fifth Cause of Action is for breach of a written contract dated December 31, 1948 (Exh. 14) and the Sixth Cause of Action is for misappropriation of trade secrets and unjust enrichment.

The original complaint was followed by an Amended and Supplemental Complaint filed August 13, 1965 (Ct 134) containing substantially the same six causes of action with some amendments, a notable one of which is an allegation of ownership of the Barrister Bond registration No. 274,875. But there is no evidence in the case of plaintiff-appellee's ownership of it as of August 13, 1965.

The issue is raised in the Second Amended Answer, filed

August 25, 1967 (Ct 148) containing a counterclaim for cancellation of Registration Nos. 655, 848 and 274, 875, jurisdiction being based on 15 U. S. C. §§ 1119 and 1121.

The First Amended Reply to counterclaims was filed July 27, 1967.

The second suit (Appeal No. 22489A) for misrepresentation, untrue statements and false advertising of stationery goods was commenced by the filing of a complaint (Ct 221) presented as a single cause of action, on March 16, 1966, in which jurisdiction was invoked under the Lanham Trademark Act of 1946, and on the ground of diversity of citizenship. This was followed by the filing on July 27, 1966 of a Second Amended Complaint (Ct 291) in which three causes of action were alleged, the first for false representations under the Lanham Trademark Act of 1946, the second differing from the first in that the false advertising is designated as unfair competition and with jurisdiction alleged on the ground of diversity of citizenship as well as under the Lanham Trademark Act, and the third differing from the second in substituting the term "untrue statements" for the term "false advertising".

The Answer to this Second Amended Complaint (Ct 304) was filed August 22, 1966.

The District Court entered its Memorandum of Decision of both cases on December 5, 1967 (Ct 461) containing its findings of fact and conclusions of law and also on December 5, 1967 entered its judgment thereon (Ct 479) granting an injunction and

an award of damages and attorneys' fees in favor of the plaintiff. On January 3, 1968, within thirty days following the entry of the judgment, the defendants-appellants filed their Notice of Appeals in the two cases (Ct 501) and an appeal bond and an Amended Designation of Record on Appeal (Ct 511).

The plaintiff filed its notice or cross-appeals (Ct 506) in the two cases from those portions of the judgment which permit defendants' limited use of the word "Friend" and which failed to award the defendants' profits to the plaintiff.

Jurisdiction of this Court is invoked under 15 U. S. C. §1121.

THE PARTIES

The personalities involved in these suits are four brothers named Friend, all of whom had been, for a period of time prior to the year 1949, together with their father Harley A. Friend who died in 1959, partners in the partnership named H. A. Friend and Company located in Zion, Illinois.

The plaintiff-appellee, H. A. Friend and Company, Inc., an Illinois corporation located in Zion, Illinois, is a successor of the partnership named H. A. Friend and Company, and its sole owners, officers and directors are the three youngest of the brothers, namely, Richard (born 1916), Howard (born 1919) and William Friend (born 1923) (Adm. 1, Ct 72). The plaintiff corporation contends that "Friends", "Barrister" and "Banner"

are trademarks which it owns, and which have been infringed by defendants-appellants.

Defendant-appellant Wilber H. Friend, nicknamed "Web", the eldest of the four brothers (born 1910) is the sole proprietor of the individual proprietorship, Friend Paper Company, and is the principal owner and officer of defendant-appellant Friend and Company, a California corporation. They have their place of business in Pasadena, California.

CONCISE STATEMENT OF THE CASE

In the first case (Appeal No. 22489), the Complaint complains of defendants-appellants' use of the business names Friend and Company, Friend Paper Company, and the word "Friend" or "Friends", "Barrister", "Banner", on or in connection with the defendants' stationery products, and alleged misappropriation of plaintiff's trade secrets, such as customer lists and materials.

After commencement of preparation of a pre-trial conference order in the first case, the plaintiff-appellee filed its second suit, Civil Action 66-470-WPG, alleging misrepresentation by the defendants-appellants of the cotton fiber content of some of their stationery products in their promotional material to customers.

The first suit arises from relationships and acts of two central figures, Harley A. Friend and his eldest son Wilber H. Friend, over approximately two decades, from the early 1930's to 1949 when Harley A. Friend was in control of H. A. Friend

and Company (as its sole proprietor up to 1941 [plaint's Adm. No. 5, Ct 74] [Wilber Friend Rt 308, 310, 311], and as the controlling partner of the partnership H. A. Friend and Company from 1940 on [Rachel Paxton dep. p. 1; p. 4, line 12 - p. 5, line 2; p. 9, line 9 - p. 10, line 10, Exh. 304, also marked Exh. AZ; Rt 212 and 430]); although Wilber H. Friend had the title of general manager after 1940 [Rt 311], Harley was "the boss" and "ran the place" (Paxton Dep. pp. 1, 4, 5, 9, and 10 above).

The evidence shows that none of the three brothers, Richard, Howard or William Friend was present during any discussions between Harley and Wilber Friend significant to this case and that they have no personal knowledge of pertinent events, acts or relationships prior to 1949, nor of such accommodations as had been arrived at between Harley and Wilber Friend by which their differences were laid to rest since 1948. The first of the two suits was commenced after Harley's death some 15 years or more after the acts complained of in the Complaint which was based on events or acts as to which Harley Friend had been informed and alerted as early as 1948.

Facts pertinent in these appeals are as follows:

In 1908 Harley A. Friend together with Joseph Friend, who was Harley's father, and a person named J. A. Friend, who was no blood relative of Harley or Joseph Friend, formed a partnership of the name "Friend Brothers", which engaged in an office supply business in Zion, Illinois; the name "Friend Brothers" being a misnomer as none of its partners was a brother

of any other (Par. 27, Pretrial Conf. Order Ct 452). This "Friend Brothers" partnership went out of business in or about 1912. After working for several years as an employee of another company, Harley Friend commenced as sole proprietor a stationery and office supply business in Zion, on about 1918 to 1920, with the name H. A. Friend and Company, which was the original predecessor of H. A. Friend and Company, Inc.

In the latter part of the 1920's defendant-appellant Wilber H. Friend became employed part-time by his father in the H. A. Friend and Company business, which employment became full-time around 1930, after he left school; and in 1941 Harley, Wilber, Richard and Howard Friend formed a partnership with the same name H. A. Friend and Company as successor to Harley's sole proprietorship, and William later became a partner in about 1945. The partnership consisting of the four brothers and their father continued until December 31, 1948, when it was dissolved following a dispute between Wilber Friend and Harley Friend. This dissolution was embodied in a written agreement dated December 31, 1948 (Exh. 14) of which the only parties were Harley Friend and Wilber Friend, and by which Wilber Friend withdrew as a partner and assigned to Harley Friend all of Wilber's interest in the partnership in consideration of a sum of money to be paid by Harley to Wilber Friend. There is no evidence that Harley Friend ever assigned to H. A. Friend and Company the interest he purchased from Wilber Friend.

Subsequent to December 31, 1948 the business of H. A.

Friend and Company was continued under the same name, as a partnership consisting of Harley A. Friend and the three younger brothers Richard, Howard and William Friend, until the formation of the plaintiff corporation H. A. Friend and Company, Inc. in 1961 which became the successor to the previous partnership H. A. Friend and Company, and the assignee of its business (Pltf's Adm. No. 29, Ct 80).

In the early 1930's appellant Wilber H. Friend, while employed by his father at H. A. Friend and Company, formed the entity named "Friend Paper Company" which at all times has operated as a wholesale paper merchant, buying stationery paper from paper mills and reselling it to customers in the retail business.

Wilber H. Friend, from the commencement of Friend Paper Company, considered it and operated it as his sole proprietorship, and has testified to this effect (Rt 38, 301, 302) and also that his father knew of it, discussed it with him, and was willing to do business with him (Rt 311). Plaintiff-appellee does not dispute that Friend Paper Company has been the sole proprietorship of Wilber H. Friend since the partnership dissolution on December 31, 1948, but asserts, contrary to the position of Wilber H. Friend, that prior to December 31, 1948 the Friend Paper Company was in reality a part of the partnership H. A. Friend and Company and the earlier sole proprietorship of the same name, and that Wilber H. Friend was operating it on behalf of H. A. Friend.

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It appears that paper mills are reluctant to sell paper directly to retailers such as H. A. Friend and Company (although the mill, Gilbert Paper Company, did sell direct to H. A. Friend and Company for a period of time [Pltf's Adm. 6, Ct 193]), and prefer to sell only to wholesalers from whom retailers must buy. Defendant-appellant understands the plaintiff-appellee's position to be that at the time in the early 1930's when H. A. Friend and Company was the sole proprietorship of Harley A. Friend, he caused Friend Paper Company to be formed as a "front" to create the appearance to those outside of H. A. Friend and Company that Friend Paper Company was a wholesale paper merchant separate from H. A. Friend and Company, in order to induce paper mills to sell directly to Friend Paper Company, and that Wilber Friend was simply performing one of the duties of his position as his father's employee in buying the paper from the mills and billing his father only what the mill charged him.

Regardless of where the ownership of Friend Paper Company lay, the facts are that Wilber H. Friend caused the name Friend Paper Company to be listed annually as a paper merchant in Lockwood's Directory for the Paper and Allied Trades (which is the principal trade journal for the stationery paper industry), in which paper manufacturers and wholesale paper merchants may list by mark or name the papers which they have available for sale (pp. 4-8 of Exh. B).

Beginning in the 1930's, Friend Paper Company has been listed annually in the said Lockwood's Directory (Rt 325, 326).

Exh. B, pages 4-18 comprise title pages with pages of the Lockwood's Directory of 1936, 1948, and 1964, respectively, which are examples of the annual directory. These exhibits show listings by Friend Paper Company of "Barrister Bond" (p. 708, 1936 Directory; p. 851, 1948 Directory; and p. 1138, 1964 Directory), and of "Friends" (p. 776, 1936 Directory; p. 919, 1948 Directory; p. 1178, 1964 Directory), and of "Banner Bond" (p. 850, 1948 Directory; p. 989, 1950 Directory; p. 1187, 1964 Directory).

From the early 1930's to the present time Wilber H. Friend operating as Friend Paper Company has ordered paper from paper mills for which he paid the mills from his own bank account under the name Friend Paper Company, and sold it to customers who paid him, as Friend Paper Company, for what they bought (Rt 318, 319). Up to the spring of 1949 most of the sales of Friend Paper Company were made to H. A. Friend and Company, which paid Friend Paper Company for them. Richard Friend, the plaintiff's president, confirmed these facts (Richard Friend dep. pp. 43, 44, 46, Exh. BH).

In reselling the paper to H. A. Friend and Company and other customers, Friend Paper Company applied a mark-up, thereby realizing a profit, and the income tax returns of Wilber H. Friend since the inception of Friend Paper Company reported his profits from the Friend Paper Company (Exh. A).

After the withdrawal of Wilber H. Friend from the partnership on December 31, 1948, he remained in the employ

of the new H. A. Friend and Company partnership at his father's request for a period of about the first three months in 1949 (Rt 36) during which time H. A. Friend and Company continued to buy its requirements of paper from Friend Paper Company as shown by Friend Paper Company's receipt of orders from H. A. Friend and Company and orders to Gilbert Paper Company for paper (Exh. X).

THE TRADEMARKS IN SUIT

During the 1920's and prior to the time when Wilber Friend first started working for his father, H. A. Friend and Company had been handling a number of types of stationery paper. Among these were unwatermarked papers referred to in advertising as "The Banner Line", and other papers which contained watermarks, including "Barrister Bond". Defendants-appellants contend that they were the first to use "Friends" as a trademark, and the Court of Appeal did not decide this point. In the 1930's when Friend Paper Company was formed, and through the 1940's, it was not apparent that H. A. Friend and Company owned the exclusive right to use any of these marks.

THE FRIEND'S MARK

Wilber Friend's first use of the word "Friends" as a watermark occurred in 1934 when he caused Valley Paper Company, a paper mill from which Friend Paper Company was purchasing, to make up a dandy roll with "Friends" on it for

impressing the watermark "Friends" on the paper (Rt 328). Following this, Friend Paper Company purchased its requirements of "Friends" watermarked paper from Gilbert Paper Company, and has continuously been purchasing and selling to its customers paper watermarked "Friends" from 1934 to the time of this suit, most of these sales having been made to H. A. Friend and Company until the spring of 1949, and after 1949 to Friend and Company in Pasadena, California, which resold it to its customers as discussed hereinafter. During discovery, plaintiff-appellee admitted that its earliest known use of "Friends" as a trademark is that represented by the brochure Exh. 10 which was published about 1938 (Rt 29).

THE BANNER BOND MARK

The mark "Banner" or "Banner Bond" has never been a watermark on a paper in the business of defendants-appellants Friend Paper Company or of Friend and Company, nor of H. A. Friend and Company at least up to the year 1949. Paper marked "Banner" or "Banner Bond" has been carried and used by many companies for a great many years and many companies have listings of it in Lockwood's Directory (Exh. B). For example, the 1926 edition of Lockwood's Directory shows several companies other than plaintiff or defendants, including Bradner Smith and Company of Chicago, listing their paper marked "Banner" (pages 2 and 3 of Exh. B). Bradner Smith and Company, a paper merchant located in Chicago, Illinois, has been handling paper marked

"Banner" ever since a time prior to the formation of H. A. Friend and Company in about 1920 (Bauder and Berg depos.; Exh. BD and BE). Plaintiff has no trademark registration of "Banner" or "Banner Bond", although it has, since the filing of the suit, applied for a registration of it in the U. S. Patent Office; and defendants have opposed the application to register it.

After defendants' move to California, unwatermarked paper supplied by Blake, Moffit and Towne in Los Angeles in boxes marked Banner has been used, as discussed hereinafter.

"BARRISTER BOND"

On May 13, 1930, Gilbert Paper Company of Menasha, Wisconsin, the paper mill from which most of the papers were acquired by Friend Paper Company and used by H. A. Friend and Company, had applied to register "Barrister Bond", and while the application was pending, assigned it to Southworth Company of Mittineague, Massachusetts, to whom registration No. 274, 875 for "Barrister Bond", in suit, issued on September 9, 1930 (Exh. 2) and its file history in the Patent Office (Exh. E) shows that Gilbert recorded in 1948 an assignment, bearing a date in December, 1930, of it from Southworth to Gilbert, following which the Patent Office republished the registration, and later renewed it, to Gilbert. It was stipulated that this re-assignment from Southworth to Gilbert occurred on December 26, 1930 (Rt 371).

In 1935, Gilbert Paper Company offered in a letter (Exh. G) to sell to Friend Paper Company, Gilbert's "Barrister Bond"

dandy rolls and all of Gilbert's rights in the "Barrister Bond" mark in consideration of Friend Paper Company reimbursing Gilbert for its disbursements. Wilber Friend did not accept Gilbert's offer to purchase the mark in 1935 (Rt 350), but continued to buy "Barrister Bond" paper from Gilbert until 1949.

On January 19, 1949, Wilber H. Friend, after his withdrawal from the partnership, and in his capacity as proprietor of Friend Paper Company, sent a letter (Exh. H) to Gilbert Paper Company requesting exclusive rights to the Barrister Bond mark. This culminated in Gilbert's invoice to Friend Paper Company dated January 21, 1949 (Exh. I) by the written terms of which Gilbert sold to Friend Paper Company exclusive rights to use of the mark "Barrister Bond", subject to Friend Paper Company continuing to purchase all papers so marked from Gilbert, this sale being effective upon receipt from Friend Paper Company of $400 which was paid by Wilber H. Friend to Gilbert (Rt 286-288). The cancelled check (Exh. J) includes the $400 (Rt 357, 358). Gilbert thereafter continued to sell paper watermarked "Barrister Bond" to Friend Paper Company for a short time up into the spring of 1949 as evidenced for example by Gilbert's invoice dated March 1949 (Exh. J).

Pursuant to the terms of the invoice Exh. I, made effective by the $400 payment, Wilber Friend as Friend Paper Company employed his attorneys, Brezina and Buckingham, to prepare a formal outright assignment of the "Barrister Bond" registration No. 274, 875 from Gilbert to Friend Paper Company, suitable for

recording in the U. S. Patent Office, as appears from correspondence (Exh. K) in February and April of 1949 between Friend Paper Company and the firm of Brezina and Buckingham and the latter's related Trademark Title Company.

Execution and delivery of such formal assignment would have eliminated the requirement for Friend Paper Company to buy its "Barrister Bond" marked paper from Gilbert, but under the written terms of the invoice provision it would have required an additional payment of $400 by Friend Paper Company. Such formal assignment free from the requirement to purchase only from Gilbert, was never executed by Gilbert Paper Company for reasons appearing hereinbelow, and accordingly Friend Paper Company never paid the additional $400 to Gilbert, beyond the first $400 which is still in the possession of Gilbert. Later, in April 1949, Gilbert requested Friend Paper Company to relinquish the exclusive rights to "Barrister Bond", which Friend Paper Company had obtained by its $400 payment, and offered to return the $400 by sending to Friend Paper Company a check in the amount of $400 (Exh. L); but Friend Paper Company did not accept the repayment check and did not agree to termination of the assignment (Rt 372, 373). Gilbert never brought any action to rescind the agreement of January 1949. But Gilbert did thereafter decline to furnish any more paper bearing the watermark "Barrister Bond" to Friend Paper Company, and Gilbert then did commence supplying paper watermarked "Barrister Bond" directly to H. A. Friend and Company.

Gilbert's refusal to abide by its invoice agreement of January 1949 with Friend Paper Company was caused by interference from Harley A. Friend. Correspondence in the latter part of 1948 and the first part of 1949 shows that Harley A. Friend was concerned about his position in respect to the several watermarked papers manufactured by Gilbert and being sold by H. A. Friend and Company which had been acquiring it from Friend Paper Company. Evidence of this concern appears in the letter dated October 7, 1948 from Gilbert to H. A. Friend and Company (Exh. M) calling Harley Friend's attention to his apparent confusion about the status of the several watermarks, including "Barrister Bond". Gilbert's position stated in that letter was that it had originally given to H. A. Friend and Company the use of the "Barrister Bond"-marked paper only in Illinois and the three states contiguous thereto, and that later Wilber Friend had been given its use in "a somewhat wider range". Gilbert's letter does not clarify whether these "uses" were exclusive or non-exclusive, but even if Gilbert did mean "exclusive", it is apparent that Gilbert implied no more than its intention that no Barrister Bond be sold to anyone else at the retail level in the designated territories (since Gilbert had not made any agreement with any of the Friend family or for any consideration), and also that the territories in question were limited to the mid-west in the general vicinity of Illinois.

During the discussions between Harley and Wilber Friend leading to the December 1948 agreement (Exh. 14), Wilber

informed his father of his intention to move either to the east or west coast (Rt 342), and also of Wilber's intention to continue the business of Friend Paper Company and with that name, after the partnership dissolution (Rt 341) and requested his father to continue giving Friend Paper Company the H. A. Friend and Company business (Rt 339). Wilber further testified of having told his father at that time of Wilber's intention to enter into the retail part of the business as well (Rt 340); and of a discussion between them to the effect that one of them would have the privilege of buying out the other and that the one bought out would have the privilege of starting up a retail business even across the street if he wished (Rt 340); and that Harley expressed his lack of interest in the east or west coasts (Rt 343); and also of having informed his father of his intention to use the name "Friend and Company" for the retail business and of displaying to him a sketch of a letterhead of "Friend and Company" (Rt 341); and that Harley made no comment when informed of Wilber's intention to continue the Friend Paper Company business and to commence the Friend and Company business (Rt 341).

There is correspondence in 1949 evidencing Harley Friend's knowledge of Wilber's intention to go into the retail business on the east or west coast and with the watermarks involved herein (Gilbert's letter of April 19, 1949 to Harley, and Harley's letter to Gilbert of April 20, 1949, Exh. N), and that Harley was aware of listings in Lockwood's Directory in connection with marks Friend Paper Company was using (Gilbert's

letter to Harley Friend of October 7, 1948, Exh. M).

By the agreement (Exh. 14) of December 31, 1948, Wilber conveyed to Harley Friend all Wilber's share of the assets, business and good will of the partnership, but the agreement is silent as to whether any trademarks or watermarks were assets or owned by the partnership or by anyone else. Neither was there any reference to Friend Paper Company nor any provision requiring any change in the business or name or products of Friend Paper Company.

Plaintiff-appellee has admitted that Wilber Friend has the right to continue the business of Friend Paper Company and with that same name after 1948 (Pltf's Adm. No. 12; Ct 76, Int. Ans. 13; Ct 125-127). Similarly, Richard Friend, plaintiff's president, conceded the right of Wilber Friend to continue Friend Paper Company (Exh. BH, p. 51, line 25 to p. 52, line 22; Rt 449) in his own choice of words: "When he left the firm he was given the name of Friend Paper Company to use." (It is defendants-appellants' position that Wilber did not need to have the name "given" to him, because he already had it.) In his testimony Richard Friend stated that he assumed that after 1948 Wilber was doing some kind of paper business as "that was what he knew and he would follow the profession", and also that he had never objected to Wilber's use of the name Friend Paper Company prior to 1963 in the line of wholesale paper. Actually he had not made objection to any kind of paper business of Wilber Friend.

Plaintiff's trial witness William Friend, the Company's

secretary, testified (Rt 544) that he knew around March of 1949 that Wilber was going to California, and that by the latter part of 1949 knew he was going into a paper business and that Wilber still carried his post office box in Zion, Illinois and "being that he said he owned Friend Paper Company, I presumed he was going into the wholesale type of business". When asked by the Court, "In the early 50's you knew he was in the paper business in California?", he answered, "Right, your Honor", and the witness further stated, "The only knowledge I had was that he was in the wholesale paper business", to which the Court asked, "That was your assumption?" and the witness answered "Yes" (Rt 545, 546).

Wilber Friend, while continuing to operate the Friend Paper Company, carried out his plan in 1949 to start up a retail stationery business similar to that of H. A. Friend and Company, on the west coast, that is, the thirteen far western states plus western Texas, as he had previously informed his father. Although nothing in the partnership dissolution agreement required this move, Wilber Friend's obvious reason for it was that he would not find on the west coast any substantial competition with H. A. Friend and Company, whose business was almost entirely in the mid-west. Its total active customers number about 6800, excluding those which have dropped out or become inactive as customers (Pltf's. Ans. to Int. 7, Ct 326). Not much more than about a hundred of these would be located in the far western states in view of the fact that the total of its customers in the far

western states, including all those who have ever discontinued as customers and including the entire state of Texas (most of which is not in the far west area served by the defendant) amounts only to about 184 (from ledger sheets, Exh. AJ and Int. Ans. 4, Ct 325). In California for example, the total of their customers, including past and inactive ones, is about 20 of which about 15 are presently active (Pltf's. Int. Ans. 3, Ct 325).

Wilber Friend bought property in Pasadena, California in 1949 for the establishment of his retail stationery business named Friend and Company, for exploitation only in the far west states of California, Arizona, Nevada, Oregon, Washington, Montana, Idaho, Utah, New Mexico, Colorado, Wyoming, Hawaii, Alaska and the western part of Texas (Lubbock, Amarillo and El Paso) where H. A. Friend and Company was virtually unknown. (Friend Paper Company, however, continued to sell to other areas including the mid-west, as previously.) At the same time he moved his Friend Paper Company business from Zion, Illinois to Pasadena, leaving in Zion only the unnamed post office box of Friend Paper Company, the purpose of which was to enable Friend Paper Company to continue to buy its requirements of stationery paper from mills located in the mid-west as had been done since the 1930's. An agent employed for the purpose took the mail from the box from time to time and readdressed it to the Pasadena office.

Documentary evidence shows that Harley Friend was kept fully informed by Gilbert Paper Company (Gilbert's letter of

April 19, 1949, Exh. N) of Wilber's intention to advertise and sell "Barrister Bond" paper in the far west, and that Wilber had purchased rights to use "Barrister Bond" from Gilbert (letter of May 4, 1949, Exh. N, Harley Friend's reply to Gilbert of April 20, 1949, Exh. N).

It was not until Gilbert's letter to H. A. Friend of October 13, 1955 (Exh. Q) that Gilbert ever offered to H. A. Friend and Company any rights to use "Barrister Bond" beyond the states contiguous to Illinois, and that letter made the offer of exclusive rights to H. A. Friend and Company for an indefinite period, subject to the purchase of more than 25,000 pounds of it per year from Gilbert, with the further right of an absolute assignment of the mark for the price of $600 in the event of future disagreement between them. This offer was not accepted by H. A. Friend and Company, and in any event would have been subject to such rights as had been purchased in 1949 by Friend Paper Company from Gilbert.

After Wilber Friend's move to California, Gilbert continued to sell to Friend Paper Company all the watermarked papers previously sold to it, excepting that in view of H. A. Friend and Company's objections, it refused to apply the "Barrister Bond" watermark to the paper previously furnished with that watermark. Instead, Wilber Friend was obliged to accept Gilbert's offer to apply the watermark "Bar-Bond". Based on his belief that he had bought from Gilbert at least the right to use the mark "Barrister Bond" for the $400 which he had paid Gilbert under the 1949

invoice (Exh. I) and also that H. A. Friend and Company did not own any exclusive rights to use "Barrister Bond", Wilber Friend boxed his "Bar-Bond" paper, which was identical to that previously marked "Barrister Bond", in boxes labeled "Barrister Bond", and sold this to Friend and Company which then re-sold it to law firm customers. Gilbert never objected to this although it was made aware of the fact that Friend Paper Company was using the term "Barrister Bond" in referring to this paper (Schmerein dep. pp. 44-45, Exh. BK).

Gilbert never refused to sell to Friend Paper Company any paper watermarked "Friends" and accordingly the Friends paper continued to be handled and sold and delivered to Friend and Company which resold it to customers.

After moving to California, Friend Paper Company obtained its requirements of the unwatermarked paper marked "Banner Bond" from Blake, Moffit and Towne, a wholesale paper merchant in Los Angeles. Black, Moffit and Towne is one of the several firms listing the availability of paper marked "Banner" in Lockwood's Directories, for example, the 1948 and 1964 Directories (Exh. B).

Friend Paper Company continued to sell its products to others than Friend and Company, as it had previously sold to others than H. A. Friend and Company prior to moving to California.

Commencing in 1950 Wilber Friend built up the business of Friend and Company from zero volume to a sales volume of

about $343,000 for the year 1966 (Exh. AI). This buildup involved a major plant investment beginning in 1950 and continuing during the '50's (Rt 438, 439). This buildup of the Friend and Company business is shown year by year by the chart (Exh. AK attached hereto as Appendix I) made from these sales figures.

The ledger sheets of H. A. Friend and Company (Exh. AJ) show that its dollar sales in the same western states where Friend and Company sells, have never been significant. From 1941 through 1949 and into the 1950's it amounted to about $1,000 or less annually, and although there was a slight increase after the mid '50's, it never reached as much as $10,000 and was never significant as compared with Friend and Company's business or with the plaintiff's total business. H. A. Friend and Company's sales performance, prepared from these business records (Exh. AJ) is shown on the chart (Exh. AK) and shows graphically the relative insignificance of their western state business.

In 1956, Howard Friend, the vice president of the plaintiff while on a trip to California, stopped twice at the office of Friend and Company at 55 West Green Street, Pasadena, and walked through the front door of Friend and Company which opens from the sidewalk. The glass door of the Friend and Company office building contained thereon at the time of Howard Friend's visit, the name "Friend and Company". Exh. AD is a photograph of this door and Exh. AE is a photograph of the same door with a sheet of cardboard placed on the inside of the door back of the name "Friend and Company" to make the name stand out better

in the photograph. This name "Friend and Company" was placed on the door in 1949 and was there unaltered until after the filing of this suit and after a deposition of Wilber Friend taken by plaintiff-appellee in March 1965 behind the same door with the name on it (Wilber Friend, Rt 398-400, Montoya dep. Exh. BJ, p. 4, lines 9-24 and p. 13, lines 10-20, Rt 455).

On April 3, 1957, the law firm of Lycette, Diamond and Sylvester in Seattle, sent a letter (Exh. AF) to H. A. Friend and Company, Zion, Illinois, which states:

> ". . . that we received a letter advising of the opening of an office at 55 West Green Street, Pasadena, California . . . ."

and also,

> "In referring back to our files, I note that the name of the company in Pasadena is 'Friend and Company', whereas your Zion firm is known as 'H. A. Friend and Company'. Perhaps we became confused in thinking the two companies were one and the same. Are we correct in assuming that the Pasadena firm is an affiliate of yours or a branch of your company?"

On April 5, 1957, H. A. Friend and Company sent a letter (Exh. AG) in reply to Lycette, Diamond and Sylvester, signed by Harley Friend, which contains the statement,

> "We are in receipt of your nice letter of the 3rd and are sorry to know any firm would follow such

a line of duplicity. However, several other customers of ours on the coast write us in this same manner . . . .

"We greatly appreciate your letter giving us this information."

Neither Harley Friend nor anyone else ever complained about the name "Friend and Company" or any other matter until August, 1963 when the firm of Brezina and Buckingham, who filed the present suit, sent its letter (Exh. AL) expressing the objections to the use of "Friend and Company" and "Friend".

The second suit is based on discrepancies discovered by plaintiff during pendency of the first suit, in Friend and Company's 1955 and 1964 catalogs (Exh. 84 and 85) and 1961 and 1964 price lists (Exh. 86 and 87). In January 1966 plaintiff's counsel called the attention of defendants' counsel to the fact that some of the papers and envelopes being sold by Friend and Company were of less fiber content than described in the catalogs. Wilber Friend conceded this to be true and stated that it arose from the fact that about a year after the 1955 catalog he changed the cotton fiber content of some of the papers he carried and that when the 1964 catalog was printed, the discrepancy was inadvertently overlooked(Rt 103, 436). In January 1966 he corrected his current price list (Exh. 87 and AS) which perpetuated the error by appropriate blanking-out of the parts containing the error (Exh. AS) and in Friend and Company's most recent price list (Exh. AT), no such errors appear (Rt 421).

It is noted that the last catalog (Exh. AT) omits items complained of by the plaintiff such as reference to "1908", "Western Division" and "Zion".

THE MEMORANDUM OF DECISION OF THE DISTRICT COURT

The Memorandum of Decision constitutes findings of fact and conclusions of law (Ct 478).

In this Memorandum (Ct 461) the District Court held: that in 1920 Harley Friend was the principal owner of H. A. Friend and Company (Ct 462); that it was H. A. Friend and Company which had caused the formation of Friend Paper Company which bought paper directly from Gilbert and sold it to the Company; that almost from its inception, the "business" of Friend Paper Company was conducted solely by Wilber, partly at his office in the headquarters of the Company with the clerical assistance of Company personnel, and partly at his home (Ct 463); that in the latter part of 1948 Wilber withdrew from, or was removed from, the Company, and his capital interest therein, including good will, was purchased by his father, and that the partnership which had included Wilber was actually dissolved on December 31, 1948 followed by the formation of a new partnership without Wilber (Ct 464, 465); that by about 1948 the Company had compiled addressograph plates bearing the names of more than 1500 lawyers and law firms in the western states and sent them a promotional brochure (Ct 465); and that in the early spring of 1949, Wilber

announced to his father and brothers his intention of moving to Pasadena, California, and engaging in the business of buying and selling paper at wholesale under the name Friend and Company and that Wilber's former partners expressed no objection to this (Ct 465).

The Memorandum referred to the 1955 and 1964 catalogs of Friend and Company (Exh. 84 and 85 respectively) and the Court criticized what it referred to as misrepresentations in the catalogs and mailings in the use of the term Western Division and of a map indicating "General Offices" at the location of Zion, and reference to the year "1908"; that these catalogs were fraudulently designed to create the impression that Friend and Company was a division of H. A. Friend and Company (Ct 466, 467); and that Wilber had tried to appropriate the good will of his father's company in western states (Ct 468).

The Memorandum held that whether Wilber Friend knew it or not, he was operating the Friend Paper Company as a fiduciary representation or a constructive trustee of H. A. Friend and Company prior to 1949; and that Wilber made no disclosure to his father or his brothers that he was using Friend Paper Company for his own benefit (Ct 471); that the understanding of Harley and the three brothers was that Wilber was operating Friend Paper Company as principal manager of H. A. Friend and Company; that such understanding was encouraged by Wilber; that Wilber acquired no individual rights in or to any of the trademarks "Friends", "Barrister" and "Banner" with which he was dealing

while he was affiliated with H. A. Friend and Company; and that insofar as the parties to this action are concerned, the entire rights in and to such trademarks remain in the plaintiff (Ct 471).

The Memorandum holds, however, that because none of Wilber's former partners raised any objection to his use of the name Friend Paper Company in 1949, when they knew about it, Wilber Friend should not be prevented from using the name Friend Paper Company in connection with the selling of paper at wholesale to stationers and other retailers (Ct 475, 476).

The Court held that the defendants have infringed on the marks "Friends", "Barrister" and "Banner" and have created confusion and that the "Friends" trademark registration No. 655, 848 is valid and subsisting insofar as the parties are concerned, and that plaintiff has been using it for many years; that plaintiff has been using its trademark "Banner" for many years and has applied to register it and that defendants have no right to use it nor oppose plaintiff's application to register it, and that H. A. Friend and Company had been using the "Barrister Bond" mark ever since prior to 1926 while it was owned by Gilbert Paper Company during which time Gilbert held it in trust for plaintiff until an assignment of it in January 1965 (Ct 472).

The Court held that the false description of the goods makes the defendants liable to the plaintiff pursuant to 15 U. S. C. §1125(a) (Ct 474); that the parties are in competition with each other in the western states, and that defendants by purporting to match the quality of the competing products while selling goods

of reduced quality and cost gained unfair advantage; and that from the standpoint of damage, there is likelihood that in future years people who have bought from defendants will become aware of the poor quality and quietly determine never again to purchase "Friend's" papers (Ct 474, 475); that it is impossible to determine the full extent to which the false descriptions have damaged the plaintiff already and will cause further injury in the future (Ct 475).

In regard to the defense of laches, the Memorandum holds: that in April 1957 Harley Friend was made aware that a law firm in Seattle had been "taken in" by Wilber's course of conduct seeking to create confusion concerning relationships between the Zion and Pasadena companies but took no action in respect to the matter nor did he inform his sons who were his partners prior to his death in 1959 (Ct 476), and the Court speculated that perhaps Harley thought the incident to be an isolated one; and that the first knowledge of Richard, Howard or William Friend of fraudulent conduct on the part of Wilber was in 1962 (Ct 476); and that under the circumstances, there was an absence of laches (Ct 477).

The Memorandum made no reference to the visit of Howard Friend to the offices of Friend and Company in 1956.

In reference to the recoverable damages and attorneys' fees, the Memorandum held that the plaintiff had been damaged; that most of the sales lost by the plaintiff to defendants were small in dollar amount but that to seek to identify them would be basically impracticable (Ct 477) but that by the interpolation, the

Court found from the evidence that plaintiff's actual damages are at least the sum of $5,000 (Ct 477), which it trebled to $15,000 under 15 U.S.C. §1117; that the misrepresentations in violation of 15 U.S.C. §1125(a) resulted in substantial injury to the plaintiff in an amount which cannot be precisely shown, but that it is not less than $20,000, which was awarded (Ct 477, 478); and that because of wilfulness of the defendants' acts calculated to trade upon the plaintiff's good will, the plaintiff was awarded $30,000 for attorneys' fees, citing National Van Lines v. Dean, 237 F.2d 688 (9th Cir. 1956). This resulted in a total monetary award of $65,000.

The judgment of the Court (Ct 479) in accordance with the findings and conclusions in its Memorandum of Decision, enjoined the defendants: from using "Friends", "Banner", "Barrister Bond", "Bar Bond", and the like; from opposing the plaintiff's application to register "Banner" as a trademark; from using the word "Friend" as a trade name unless preceded by "Wilber" and accompanied by the parenthetical phrase "Not affiliated with H. A. Friend and Company of Zion, Illinois", except that the defendants were specifically permitted to use the name "Friend Paper Company" for the business of selling paper at wholesale to stationers and other retailers of paper; from advertising, asserting or implying that defendants' business began prior to 1950 or that it has any relationship with Zion, Illinois, or that its Pasadena establishment is a division of any other company; from selling stationery of different quality than defendants shall have advertised

it. Monetary judgment was awarded to plaintiff in the total amount of $65,000 arrived at as stated above.

PRESENT POSTURE OF THE APPEALS

A factor which the District Judge is believed to have found most disturbing, and fraudulent, is the format of the 1956 and 1964 catalogs of Friend and Company, with particular reference to "1908", "Western Division", and "Zion". All these items were voluntarily changed prior to the court's decision.

It is not denied that the name Friend and Company is confusingly similar to H. A. Friend and Company, and it can be considered that neither party did in 1949 what would have been best for it. Moreover the defendants may have been unwise from an economic and business point of view, if for no other, in not using entirely different names and marks in California from anything previously used in Zion, regardless of what their legal rights were. But that is hindsight, and it is now left to determine where the rights lie.

It should be noted that Wilber Friend was brought up in a salesman's atmosphere in his father's company where some exaggerations and distortions helpful in selling the product were used: the use of "1908" although there was a discontinuity between 1914 and 1919, when Harley Friend was not an owner of any business (Rt 433-445); the name "Friend Brothers" for the 1908 business although there were no brothers in it; the use of "wholesale paper" in association with the name H. A. Friend and

Company to describe what plaintiff here insists is a retail paper business, distinct from a wholesale paper business (Rt 401, Exh. 13); and the adoption by the owners of H. A. Friend and Company of the confusingly similar name Friend Paper Products Company Ans. Int. 1, Ct 181-183; Ans. Int. 5, Ct 485) for a wholesale paper business, after conceding the name Friend Paper Company to defendants for an identical type of business which had always operated and sold in the mid-west area. If such conduct be reprehensible on the part of Wilber Friend, then it is a basis for the defendants' defense of unclean hands on the part of the plaintiff.

The worst that should be thought of Wilber Friend is that he may have outdone his father in using the Zion post office address of Friend Paper Company to puff up the expansiveness of his business. There is no evidence that he ever told, or instructed anyone else to tell, a customer that his business was connected with the plaintiff.

It is submitted that these facts should not result in the large money awards and serious injunctions in respect to the basic factors of the errors in cotton fiber content and the paper trade names, marks and watermarks, used by the defendants for a great many years without protest, and never concealed from the plaintiff, which Wilber Friend had good grounds for believing he had every right to use.

Defendants-appellants presented a counterclaim charging unfair competition and trademark infringement of appellant's exclusive right to use "Barrister Bond" and "Friends", but in the

light of the fact that no attempt was ever made to prevent H. A. Friend and Company from using these marks, this counterclaim was not seriously advocated and is not being presented here.

ASSIGNMENT OF ERRORS

The District Court erred:

1. In holding that Friend Paper Company was ever owned by, or part of, H. A. Friend and Company.

2. In not holding that Wilber Friend solely formed and owned Friend Paper Company ever since its inception in the early 1930's.

3. In holding that H. A. Friend and Company, Inc. owns any of the marks involved in this suit.

4. In holding that "Friends" and its registration No. 655,848 is a valid and subsisting trademark exclusively owned by H. A. Friend and Company.

5. In holding that "Banner" is a trademark owned exclusively by H. A. Friend and Company.

6. In holding that "Barrister Bond" and its registration No. 274,875 is a valid and subsisting trademark exclusively owned by, or held in trust for, H. A. Friend and Company.

7. In failing to hold that H. A. Friend and Company did not obtain even a purported assignment of "Barrister Bond" or its registration No. 274,875 until 1965, after the filing of this suit.

8. In not holding that Friend and Company commenced and built up its business in a geographical area substantially

separate from that of plaintiff and its predecessors.

9. In holding that there was no laches on the part of plaintiff and in not holding that laches, acquiescence, estoppel and statute of limitations are a bar to the suit.

10. In not holding that Registration Nos. 655,848 and 544,450 for "Friends" and "Friends Linen" and No. 274,875 for "Barrister Bond" should be cancelled.

11. In not declaring the right of defendants-appellants to carry on their business with the same names and marks as heretofore.

12. In not dismissing Action No. 66-470-WPG for lack of jurisdiction and for failure to state a claim for which relief may be granted.

13. In making any money award of damages to the plaintiff.

14. In awarding any attorney's fees to the plaintiff.

15. In enjoining defendants from using "Bar-Bond".

16. In enjoining defendants from using any of "Friend", "Friends", "Banner", "Barrister Bond" and "Friend and Company".

17. In enjoining defendants from opposing plaintiff's application to register "Banner" as a trademark.

18. In enjoining defendants' use of the name "Friend Paper Company" outside the wholesale paper business.

19. In enjoining defendants from asserting in any way that any of their business began prior to 1950 or ever had any relationship with Zion or that its Pasadena establishment is a division of any company.

20. In enjoining defendants from selling stationery of different quality than advertised.

21. In Specific Findings of Fact, including: that Harley did not know Wilber owned Friend Paper Company in the 1930's and thereafter, and that Wilber encouraged his father or brothers to believe otherwise; that Wilber ever operated Friend Paper Company as a fiduciary or constructive trustee for H. A. Friend and Company; that Wilber made any "announcement" to his brothers about continuing Friend Paper Company; and that the announcement to Harley was as late as 1949; that H. A. Friend and Company was not alerted or notified by April 1957, and earlier, of the Pasadena business, names and marks of Friend and Company and Friend Paper Company; that there is likelihood that in future years purchasers will become aware of poor quality of defendants' papers; and that plaintiff suffered damage.

ARGUMENT

I
FRIEND PAPER COMPANY WAS NEVER OWNED BY, OR ANY PART OF, H. A. FRIEND AND COMPANY; AND

II
WILBER FRIEND SOLELY FORMED AND OWNED FRIEND PAPER COMPANY SINCE ITS INCEPTION.

The matter of Friend Paper Company's initial ownership is here discussed because the District Court appears to have given much weight to what it considered to be Wilber Friend's breach of fiduciary

relationship with H. A. Friend and Company in the operation of Friend Paper Company, resulting in the Court finding it unnecessary to consider much other pertinent evidence which defendants-appellants regard as determinative of the issues, and which is set forth in the Assignment of Errors herein. Furthermore, it is believed likely that the Friend Paper Company matter was a factor in the severity of the award of damages and attorneys' fees to plaintiff-appellee.

The District Court's Memorandum of Decision states that by 1920, Harley Friend was the "principal" owner of H. A. Friend and Company, referred to as the "Company" (Ct 462). He was at that time, in fact, its <u>only</u> owner as well as its manager (Wilber Friend Rt 15, 26, 308, 310, 311). Wilber Friend did not become the general manager until it was provided for in the partnership agreement of December 31, 1940, although he earlier took charge of things when his father was away from the office. The Amended Complaint states, "Mr. Harley A. Friend became the sole proprietor of this business, which was called and became known as H. A. Friend and Company" (Ct 135) and "The individual proprietorship continued . . . to 1940" (Ct 136). (The Complaint alleges its inception in 1912, but the only evidence about its inception is 1918-1920.)

The Decision further states that around the mid '30's "the Company caused to be formed the Friend Paper Company, which bought paper directly from Gilbert and sold it to the Company" (Ct 463). It is submitted that there is no substantial

evidence in the case supporting this holding that the Company (which in the 1930's consisted solely of Harley A. Friend) "caused" the formation of Friend Paper Company. The only evidence on this point is the testimony of Wilber Friend (Rt 38, 39, 311) to the effect that he formed the Friend Paper Company.

In its case in chief, the plaintiff called the defendant Wilber Friend as an adverse witness, who testified (Rt 38) that: "Friend Paper Company purchased paper under the name of Barrister Bond and so forth"; that "I am the Friend Paper Company", and its place of business as "In my home" (Rt 39). Under questioning of the Court, Wilber Friend reiterated his sole ownership of Friend Paper Company "right from the beginning" (Rt 297, 302); that his father and his brother William knew he owned it, that he did not recall any discussions with his brothers about its ownership but did discuss its ownership with his father.

While it may be true that plaintiff-appellee is not bound by the testimony of defendant-appellant, it is nevertheless the fact that plaintiff-appellee rested its case (Rt 306) after calling as its other witnesses only William Friend, its corporate secretary, Harold M. Bennett, Melvin P. Poole and Dale Walker, none of whom testified about the identity or ownership of Friend Paper Company. This left Wilber Friend's testimony as the only testimony on the subject.

The only witness called by defendants-appellants was Wilber Friend who gave details of his Friend Paper Company operation and relationship with his father. He testified that at

the time of starting up Friend Paper Company "I asked him for his business and he acquiesced. He allowed me to sell my products, my goods" (Rt 311) and that it was always operated at a profit to Wilber who reported the profit in his income tax returns (Exh. A, Rt 312-315).

William Friend, recalled by plaintiff-appellee in rebuttal, testified regarding Friend Paper Company "It was just a front for buying paper through the various paper mills" (Rt 529). This testimony may represent William's mental attitude, but it does not show who owns Friend Paper Company.

When asked how he knew Friend Paper Company was merely a buying front for H. A. Friend and Company, he testified (Rt 535):

> "When I came in as a partner into the firm I talked with my brother Wilber. He asked me what I was going to do after I had gotten out of the service, and I said I would like to become a member of the firm, and he told me, well, it was a good clean business, and that we enjoyed a good business, and that we had an advantage over our competitors, being that we could buy direct."

This testimony does not state who "we" is or are, and assuming the word "we" was uttered at all, it could just as well have referred to Friend Paper Company as to H. A. Friend and Company. Wilber Friend consistently referred to Friend Paper Company as "we" (Rt 38, 39, correspondence Exhs. H, K, P, S),

and he used the "we" in testimony in this case (Rt 38). It is submitted also that this attempt to paraphrase a sentence out of a conversation in 1945, twenty-two years previously, is in itself a reason to treat it with suspicion.

In regard to the profits of Friend Paper Company, William Friend testified, "I did not know of any profits to be made" (Rt 529). This signifies only that he does not know whether or not profit was to be made. The witness' attempt to state what his father and other brothers knew was stricken. He testified (Rt 539):

> "We assumed that he was not making a profit all those years" and "My two brothers and my father assumed that he wasn't."

This testimony, in addition to being mere "assumption", was stricken in reference to the two brothers and father on the ground of hearsay (Rt 539, 540).

William Friend's lack of knowledge about the inception of Friend Paper Company is shown by the following testimony (Rt 536):

> "Q. You don't know anything about the inception of Friend Paper Company?
>
> "A. Only what came up at the time of the dissolution.
>
> "Q. You mean what other people told you?
>
> "A. Right."

The witness did not attempt to assert anything he might have heard about Friend Paper Company's inception. It is

submitted that there is no substantial evidence that Friend Paper Company ever had the same identity as H. A. Friend and Company.

A finding of the District Court should be reversed and set aside where there is no substantial evidence to support it, or where it is clear that a mistake has been committed. Lassiter v. Guy F. Atkinson Co., 176 F. 2d 984, 993 (9 Cir. 1949) quoting from United States v. U. S. Gypsum Co., 333 U. S. 364, 395, 68 S. Ct. 525, 542, 92 L. Ed. 746; Vice v. Thacker, 30 Cal. 2d 84, 180 P. 2d 4 (Calif. S. Ct. 1947); or unless it is against the clear weight of the evidence. Cleo Syrup Corp. v. Coca-Cola Co., 139 F. 2d 416, 417, 418 (8 Cir. 1943), cert. denied 321 U. S. 781, 64 S. Ct. 638, 88 L. Ed. 1074.

It is noteworthy that the only one of the Zion branch of the Friend family produced at the trial was William Friend, the youngest brother, and therefore having the least knowledge. During discovery, the defendants-appellants took the deposition of Richard Friend, plaintiff's president, and the oldest of the Zion brothers, because he was present at H. A. Friend and Company during the 1930's as well as the 1940's, although in the early 1930's he did only part-time work there. Defendants-appellants took his deposition rather than that of William Friend because Richard Friend had the most knowledge of the pertinent events. Wilber Friend testified that his father and his brother Richard visited the place of business of Friend Paper Company at his apartment "all through the '30's", his father frequently and his

brother Richard less frequently (Rt 320, 321). It should be regarded unfavorable to the plaintiff-appellee that it chose to produce at the trial the least knowledgable one of the Friend brothers to refute the testimony of Wilber Friend in the matter of Friend Paper Company.

The statement in the Decision (Ct 463) that "Almost from its inception its 'business' was conducted solely by Wilber", contains an implication that in its initial stage, someone else, presumably Harley A. Friend, conducted the Friend Paper Company either in whole or in part. But there is no evidence in the case that anyone other than Wilber Friend conducted this business; and there is evidence that Wilber owned and conducted it (Wilber Friend, Rt 311; Wilber Friend Rt 528). He paid the expenses of Friend Paper Company (Rt 314) and paid the mills for the paper he purchased, from his own bank account (Rt 318, 319) and in selling the paper to his customers, the principal one of which was H. A. Friend and Company, he applied a markup and made a profit (Rt 312-315). His customers included others than H. A. Friend and Company, represented in Exh. Y (Rt 383, 384), page 5 of which is an invoice representing merchandise shipped to Weber Fly Company of Stevens Point, Wisconsin, and page 7 of which represents a purchase from Friend Paper Company by Paper Box and Specialty Company, for example (Wilber Friend Rt 384). His income tax returns, Exh. A, show that he reported the Friend Paper Company profits throughout the years beginning as early as 1934. The office of Friend Paper Company was at his home where

he did the work by use of office equipment located there (Rt 319). He maintained a post office box in which Friend Paper Company's mail was received.

The Decision further states in reference to H. A. Friend and Company "its stationery was also advertised as 'Friend's Papers', and more particularly as 'Friend's Typewriter Papers', 'Friends' Legal Linen', and the like" (Ct 464), in the period prior to the formation of the partnership in 1941. This advertising refers to the brochure Exh. 10 published about 1938. But Friend Paper Company, ever since the early 1930's was advertising its Friend's papers in Lockwood's Directory, the principal advertising medium of wholesale paper merchants, and plaintiff-appellee knew about this (Exh. BH); and also Gilbert's letter to H. A. Friend on October 7, 1948 covering Barrister Bond and other marks (Exh. M) stated: "The word Plymouth is recorded in Lockwood's Directory by a number of people . . . ."

There is no evidence that H. A. Friend and Company sold paper bearing a "Friend" or "Friends" trademark any earlier than Friend Paper Company did. Wilber Friend testified (Rt 328) that the first use of "Friends" in a watermark occurred in 1934 when he, as Friend Paper Company, arranged with Valley Paper Company of Holyoke, Massachusetts, for them to make a dandy roll containing the word "Friends" to impress it as a watermark on the paper sold to Friend Paper Company. During discovery, plaintiff stated that its first use of "Friends" is represented by the brochure Exh. 10 first published about 1938 (Rt 29), and Richard Friend

confirmed this (Richard Friend dep. p. 70, line 17 to p. 72, line 17 and p. 81, line 16 to p. 82, line 5, Exh. BH).

At the trial, however, plaintiff-appellee introduced a document (Exh. 282) referred to as a more recently discovered invoice bearing a date in May, 1931 apparently purporting to represent a sale by H. A. Friend and Company of paper called "Friends", but considered by defendants-appellants insufficient to show a trademark use, because it is not evidence that "Friends" appeared on the paper or its container, required for a trademark use, and is certainly not evidence of the existence of a watermark "Friends". The witness William Friend had no personal knowledge of its inception or what it represented, and defendants-appellants' objection on the ground of not being proven was overruled (Rt 262-267). The same objection is renewed here, in view of Richard Friend's deposition testimony and plaintiff-appellee's admission that the brochure Exh. 10 was the earliest evidence. Moreover the "Friends Linen" Registration No. 544, 450 (Exh. T) claims first use on June 30, 1949 which is inconsistent with a 1931 date of use.

The Decision states (Ct 471):

> "The evidence clearly shows that Wilber made no disclosure to his father or his brothers that he was using Friend Paper Company for his own benefit."

There is such evidence insofar as such disclosure to the trial witness William Friend is concerned, but there is no such evidence insofar as disclosure to Harley Friend is concerned. The evidence shows that Wilber Friend's business conversations were mostly

confined to discussions with his father rather than with his youngest brother. This was a natural result of the situation where Wilber, the eldest brother, was performing an important part of the operation before the three younger brothers acquired much knowledge of the business. Harley Friend was "the boss" and in full control and controlled Wilber even though Wilber Friend was given the duties and even the title of general manager of the plant operation in December 1940. Any possible doubt about this is dissipater by the plaintiff's own witness Rachel Paxton who told in her deposition (Exh. AZ) of having been employed by H. A. Friend and Company from September 1939 to July 1941, and testified that "Harley was the boss" and "ran the place" (Dep. pp. 3, 4, 9, 10).

As further evidence of Harley's control is Wilber Friend's testimony that his father had told him in the latter part of 1948 that either one could buy out the other, with the result that Wilber was bought out by Harley Friend (but not by any of the brothers) (Rt 340). Furthermore, all correspondence of H. A. Friend and Company in evidence here (Exh. M, N, O, AG) prior to Harley's death, relating to matters involving Harley Friend and Wilber Friend in 1948 and 1949, is signed by Harley Friend and none of it is signed by any of the other three brothers.

There is no substantial evidence that Harley never knew that Wilber owned Friend Paper Company or that Wilber failed to so inform him. Wilber Friend's testimony is that his father was aware of Wilber's ownership of it (Rt 311, 321). The very fact

that Harley Friend greeted with silence Wilber's announcement at the end of 1948 that Wilber intended to continue the Friend Paper Company business is in itself a tacit admission that Harley knew Wilber was its owner prior to December, 1948. Further confirmation of this fact appears in pages 54 and 55 of the deposition of Richard Friend, plaintiff's president (Exh. BH), who testified:

> "Q. Did you know the name of his business in California?
>
> "A. I don't know. I assume it was Friend Paper Company. . . .
>
> "Q. That when he was given the name of Friend Paper Company in 1948 he was thereupon doing business, doing some kind of paper business. Is that right?
>
> "A. Yes. We would assume that; that was what he knew and he would follow the profession."

The Decision also states (Ct 471):

> "Their understanding, which Wilber carefully encouraged, was that he was operating Friend Paper Company as part of his function as principal manager of H. A. Friend and Company, and that the former was being operated solely for the benefit of the latter."

It is submitted that there is no substantial evidence supporting this quoted portion of the Decision. The only testimony at the trial by the plaintiff-appellee which could refer in any way to this was the above quoted testimony of William Friend, at Rt 529

concerning competitive advantage. The mere fact that Wilber was making a profit did not negate the competitive advantage to H. A. Friend and Company of his direct buying from the paper mill, for it is entirely possible, and even probable, that Friend Paper Company was applying less of a markup in selling to H. A. Friend and Company than had been obtainable from other wholesalers. It would be incredible if Harley A. Friend, in switching from Moser Paper Company to Friend Paper Company for his purchases in the 1930's, was not aware that he was getting a better buy from Friend Paper Company, which was the reason for his buying from Friend Paper Company in the first place. At Ct 539, the witness William Friend was asked:

> "Q. When did you learn that he was not supposed to make a profit?
>
> "A. We assumed that he was not making a profit all those years.
>
> "Q. You just assumed it?
>
> "A. My two brothers and my father assumed that he wasn't."

This last answer about the two brothers and father was stricken out as hearsay (Ct 540), and as for William it was an assumption only and not a fact.

It is submitted that such testimony as to who was the proprietor of Friend Paper Company, based only on conclusions and assumptions of the witness William Friend and attempted hearsay evidence, is not substantial and does not overcome the

testimony of Wilber Friend to the contrary, supported by the documentary evidence of his income tax returns showing the profits, the admissions that he did profit, his advertising of Friend Paper Company's watermarks to the trade, and his sales to other customers, and the circumstance of Harley Friend maintaining silence when informed of Wilber's intention to continue with Friend Paper Company. The vague testimony of William Friend as to some business of Friend Paper Company, such as calls by paper mill salesmen and the typing of some letters on the premises of H. A. Friend and Company does not refute this, and is not inconsistent with that part of the 1941 partnership agreement referred to by the Court, providing for the partners to work full-time for the partnership. It is well known that persons employed full-time habitually engage in some personal errands or business during a working day.

III

H. A. FRIEND AND COMPANY DOES NOT OWN ANY OF THE MARKS INVOLVED IN THIS SUIT.

A pertinent question is: does H. A. Friend and Company own and have the right to exclude others from any, or all, of the "Friends", "Barrister" and "Banner" marks for stationery paper? It is submitted that it does not; and that therefore it does not have the right to exclude defendants-appellants from their use.

H. A. Friend and Company has <u>used</u> stationery paper marked "Friends", "Barrister" and "Banner", but the mere fact of <u>use</u> is not tantamount to <u>ownership</u>; that is, the right to exclude others from use. The evidence is that others have "used" these marks also. Gilbert Paper Company, the paper mill, used the watermarks "Barrister" and "Friends" in manufacturing and selling stationery paper to wholesale paper merchants, for example, Moser Paper Company, and Friend Paper Company.

It is conceded that it would be possible for a retailer or a wholesaler to become the owner of a watermark made and sold by a paper mill, but only by some contractual arrangement as to ownership of the mark.

In the present case there is no evidence of any arrangement as to <u>ownership</u> of watermarks by H. A. Friend and Company with Gilbert Paper Company, the mill, or Moser Paper Company or Friend Paper Company. There is no evidence that Moser Paper Company or H. A. Friend and Company handled

"Friends"-watermarked paper before Friend Paper Company did.

"Banner" was never used as a watermark by either of the parties to this suit. The paper called "Banner" is a plain, unmarked paper which has been sold by placing it in cartons bearing the mark "Banner Bond." H. A. Friend and Company's use of "Banner" has never been exclusive, as shown by the testimony of Bauder and Berg to the effect that Bradner Smith and Company, a wholesale paper merchant of Chicago, Illinois, has been handling, since prior to 1921, stationery paper marked "Banner" (Bauder and Berg depos., Exh. AM and AO, Rt 417).

Bradner Smith and Company has listed its "Banner" paper in Lockwood's Directory through the years (Exh. B) along with a number of other paper merchants who have listed their "Banner"-marked paper in Lockwood's Directory (Exh. B, pp. 2, 5, 6, 9, 12, 16).

Both the "Friends" and "Barrister" marks have been listed in Lockwood's Directory since the early 1930's by Friend Paper Company, (Exh. B, pp. 7, 9, 10, 13, 14, 17, 18).

IV

PLAINTIFF-APPELLEE DOES NOT OWN THE "FRIENDS" REGISTRATION NO. 655,848.

Specific reasons why H. A. Friend and Company does not own "Friends" or a valid registration for it are:

(a) Friend Paper Products Company, a

wholesale paper merchant, is its owner, if anything is owned.

(b) H. A. Friend and Company abandoned whatever ownership it had, if any.

(c) "Friends" is primarily merely a surname.

(a) Friend Paper Products Company, a wholesale paper merchant, is its owner, if anything is owned.

The "Friends" registration No. 655,848 is for "Bond, Parchment, and Linen Papers." Richard W. Friend, plaintiff's president, testified in October 1964 by discovery deposition that this registration is owned by Friend Paper Products Company, a partnership consisting of Richard, Howard and William Friend. The gist of his testimony is as follows:

"MR. ANGUS: Then Friend Paper Products Company owns the registration; is that correct?

"THE WITNESS: On record. That is what the record shows." (Exh. BH, p. 95, lines 21-24).

"Q. Mr. Friend, is the Friend Paper Products Company still in existence?

"A. It is.

"Q. That is the partnership, isn't it?

"A. That is the partnership."

The file wrapper and contents of the "Friends" trademark application (Exh. V) shows that on July 26, 1963 Friend Paper Products Company, the wholesale paper merchant, filed an

affidavit under Lanham Act Sections 8 & 15 (required for continuing the registration alive), alleging continuous use of the mark. There is no allegation of use by the retailer, H. A. Friend and Company, and the affidavit implies that the more than five years' continuous use referred to therein was by Friend Paper Products Company which had been buying the paper from Gilbert Paper Company and reselling it, since 1949. As shown at pages 86-97 of this deposition of Richard W. Friend, (Exh. BH), Friend Paper Products Company was never the same partnership as plaintiff's predecessor partnership named H. A. Friend and Company, and it never had any identity with the plaintiff corporation H. A. Friend and Company, Inc.

When the Patent Office questioned the ownership of the registration of Friend Paper Products Company, in Paper No. 5 of the file wrapper, Exh. V, the attorney who submitted the affidavit asserted that Friend Paper Products Company was simply a new name for the partnership H. A. Friend and Company. This assertion of the attorney was erroneous because of: the contrary testimony of Richard W. Friend, above; and also the fact that the partnership, H. A. Friend and Company, ceased to exist in 1961 upon the formation of the plaintiff corporation, H. A. Friend and Company, Inc., which succeeded to it, while the wholesaler Friend Paper Products Company, a partnership, has continued to the present time.

If it were not for this misrepresentation of the identity of Friend Paper Products Company to the Patent Office, the Sec.

8 & 15 affidavit would not have been accepted by the Patent Office, and the registration would have lapsed in 1963 at the end of six years from the registration date, under the Lanham Act Sec. 8(a) (15 USC 1058a) (Appendix II). It is submitted that this court should accordingly hold the registration lapsed.

(b) H. A. Friend and Company abandoned whatever ownership it had, if any.

H. A. Friend and Company's concession made at least as early as 1949 (Ct 76, 125-127) and the District Court's finding (CT 475) that Wilber Friend owns the right to continue the operation of Friend Paper Company as before, and with the name, as his sole proprietorship, negates any ownership, that is, exclusive right, in H. A. Friend and Company to "Friend" as a trademark for stationery paper, even if it could have had such right prior to 1949, which defendants-appellants deny. Since Friend Paper Company's business is the selling of stationery paper, the very goods for which Registration No. 655, 848 was issued, it is not possible for H. A. Friend and Company to obtain a valid registration for it on its application to register in the Patent Office, filed in 1957. The application for the registration of "Friends" required the affidavit statement (Exh. V) that no one other than the application has the right to use "Friends", and if the Patent Office had known that this statement was incorrect, it would not have issued the registration. It is submitted that this Court should hold it invalid. The right to use the name

Friend Paper Company for a paper product establishes Friend Paper Company's right to refer to its paper as "Friend" or "Friends" paper and to advertise it as such (Exh. B_1-B_4). Since "Friends" is simply the possessive form of "Friend", "Friends" is in no different position than "Friend" in this respect.

Not only does the long continued use of the name Friend Paper Company bar any exclusivity to the plaintiff-appellee in "Friend" or "Friends", but also the very use ever since 1948 (and ever since the 1930's by defendants-appellants' contention) of the name Friends on the paper products handled by Friend Paper Company is a bar to the validity of Registration 655, 848 under Lanham Act Sec. 2(d) (15 USC 1052) (Appendix II); for no one can validly register a mark which has long been used by another in a trade name or trademark in a proper or permissive manner for the same kind of goods. If plaintiff-appellee's ownership of "Friends" or its registration were valid, it would necessarily follow that it would have the right to exclude defendants-appellants from making any use of "Friend" or "Friends", including the name Friend Paper Company, because a valid trademark cannot be validly used by another as part of his trade name. If plaintiff-appellee ever had any exclusive right to "Friend" or "Friends", it abandoned that right by conceding at least as early as 1949 that Friend Paper Company and its name and business belong to Wilber Friend.

The "Friends" registration should have been refused because it resembles the trade name Friend Paper Company,

used since the early 1930's and not abandoned (Lanham Act Sec. 2(d)). The earliest evidence of trademark use of "Friends" by plaintiff-appellee is the brochure, Exh. 10, first distributed and published about 1938, following the formation of Friend Paper Company (Rt 29).

Acquiescence or permission in another's use of a mark, and even a mere idly standing by without protest or legal action, for a long time constitutes an abandonment of a trademark. French Republic, France Sec. CSS Corp. v. Saratoga Vichy Spring Co., 191 U.S. 427, 48 L.Ed. 247, (1903); Nebraska Consolidated Mills Co. v. Quaker Oats Co., 115 USPQ 85 (Comm. of Patents, 1957); R. L. Bennett & Sons v. Farmers Seed and Gin Co., 288 F. 365 (CA 5, 1923) Appendix II); Callmann on Unfair Competition and Trademarks, 2nd Edition, published 1950, Volume 3, p. 1338 (Appendix II).

In International Silver Co. v. Oneida Community, Ltd., 73 F.2d 69 (CA 2, 1934), the predecessors of the plaintiff were the first to use "Rogers" for their silver business, but the defendant or its predecessors had been using "Rogers" in its silver business for some 30 years with the knowledge of plaintiff; and the plaintiff had made purchases of goods from defendant's predecessors who used "Rogers" in their trade name. The court held that these facts precluded the plaintiff from having the exclusive right to "Rogers" and that the defendant was free to use it also.

(c) "Friend's" is Primarily merely a surname.

It is a basic rule that trademark infringement or unfair competition cannot be predicated on a bona fide use by an individual of his own name in his own business, even though such use may incidentally interfere with or injure the business of another person or organization of the same or similar name. Lanham Act Sec. 2(e) (3) (Appendix II); American Distilling Co. v. Bellows and Co., 102 CA 2d. 8, 226 P. 2d 751 (1951).

A further requirement is that a plaintiff's name must have acquired a secondary meaning before he can prohibit its use by another. Tomsky v. Clark, 73 CA 412, 238 P. 950 (1925); Academy of Motion Picture Arts and Sciences v. Benson, 15 C. 2d 685, 690 (1940) (Appendix II); Locatelli, Inc. v. Tomaiuoli, 129 F. Supp 630, 104 USPQ 332 (DC NJ, 1955); Fish Bros. Wagon Co. v. Fish Bros. Mfg. Co., 95 F. 457, (CA 8, 1899).

In Visser v. Macres, 214 CA 2d. 249, 137 USPQ 492 (1963), the court held for the plaintiff, but only because the family name "Macres" had acquired a secondary meaning in the City of Anaheim where the controversy was centered.

Surnames are registerable on the Principal Register provided they are brought within the provision of Lanham Act Sect. 2(f) which provides that "nothing herein shall prevent the registration of a mark used by the applicant which has become distinctive of the applicant's goods in commerce. The Commissioner may accept as prima facie evidence that the mark

has become distinctive, as applied to the applicant's goods in commerce, proof of substantially exclusive and continuous use thereof as a mark by the applicant in commerce for the five years next preceding the date of filing of the application for its registration (15 USC 1052)." H. A. Friend and Company could not have submitted valid "proof of substantially exclusive and continuous use" during the five year period ending February, 1957, for the reason that Friend Paper Company, as well as Friend and Company, were using "Friend" in their trade names and were using paper marked "Friends" continuously during that period. Plaintiff's registration should never have been granted and it is invalid. Graff Co. v. Cook Co., 2 F.2d 938 (Ct. of Appeals, DC 1924); Spencer v. V.D.O. Instruments, Ltd., 232 F.Supp 735, 142 USPQ 72 (ED Mich. 1964).

The Friends Registration is Not Incontestable.

Plaintiff-appellee has asserted that Registration No. 655,848 has acquired an immunity from attack on the ground that it has acquired a Lanham Act incontestability under Lanham Act Sec. 15 (15 USC 1065) (Appendix II) by reason of having been in existence for more than five years after the registration date; but provisions of the Lanham Act, considered with the actual facts, deprive it of incontestible status. Sec. 15 even if complied with does no more than guarantee the registrant's right to use the mark for the goods, but does not grant any right to exclude others.

One of the exceptions set forth in Sec. 15 negating the

status of incontestability is subsection (c) of Sec. 14 (15 USC 1064) which reads:

> "Sec. 14 Cancellation of Registrations.
>
> Any person who believes that he is or will be damaged by the registration of a mark on the Principal Register . . . may . . . . apply to cancel said registration . . . .
>
> (c) At any time if the registered mark . . . . has been abandoned or its registration was obtained fraudulently . . . . . ."

Sec. 33(b) (15 USC 1115(b)) does provide that the registration certificate of a mark which has acquired an incontestable status is conclusive evidence of the registrant's right to exclude others, provided certain conditions are met, namely, (1) that the registration or the incontestable status were not obtained fraudulently; (2) that the mark has not been abandoned by the registrant; (4) that the use of the name [Friend and Company] . . . charged to be an infringement is a use, otherwise than as a trade or service mark, of the party's individual name in his own business, or of the individual name of anyone in privity with such party [Wilber Friend is in privity with Friend and Company]; (5) that the mark [Friends] charged as an infringement was adopted by the alleged infringer without knowledge of the registrant's prior use [of Friends] and has been continuously used by the alleged infringer from a date prior to the date of the publi-

cation of the registered mark, in the area of the continuous use [through the United States by Friend Paper Company since 1934 (and since 1948) and in the far western states by Friend and Company since 1950].

V

H. A. FRIEND AND COMPANY DOES NOT OWN "BANNER" AS A TRADEMARK

Long prior to any date of use of "Banner" or "Banner Bond" as a trademark by H. A. Friend and Company (Exh. 10, 1938), others were using "Banner" for stationery paper. Bradner Smith and Company has been continuously selling paper in an area within a 300 mile radius of Chicago, (H. A. Friend and Company's area), with the mark "Banner" ever since before 1921, and is still selling it. (Bauder dep. pp. 3-6; p. 10, line 8 to p. 11, line 3; p. 13, lines 9-15; p. 14, lines 5-16; In evid. Rt 417; Berg dep. pp. 18-24; In evid. Rt 417). Pages 68 and 69 of Bradner Smith and Company's June 20, 1925 catalog (Exh. AM) show the advertising of "Banner" Manifold, 500 sheets in package. (Exh. AM is Bauder dep. Exh. 1; Rt 417). Exhibits AN and AO (Bauder dep. Exh. 2 and 3 respectively; Rt 385, 417) are labels marked "WhiteBanner Manifold" and "Banner Manifold", respectively, used by Bradner Smith and Company for its papers. Bauder acknowledged the listings of Bradner Smith and Company annually in Lockwood's Directory as represented by the 1926 Directory and 1948 Directory (Exh. B_4 and B_2) (Bauder dep. p. 15,

line 12, to p. 16, line 20; Rt 417). Many others have listed Banner in Lockwood's (Exh. B_1-B_4).

Friend Paper Company has listed Banner Bond in Lockwood's Directory since the 1940's, for example, the 1948 Lockwood, Exh. B.

Under the provision of Lanham Act Sec 2(d) (15 USC 1052) H. A. Friend and Company is not entitled to register "Banner" in view of this long continuous use and advertising of it by Bradner Smith and Company and by Friend Paper Company and the others; and its conduct in not even applying to register it until 1965, obviously only for the purpose of this suit filed in 1964, is a strong indication that plaintiff-appellee does not have, and never considered it had, exclusive rights in "Banner." Clearly Banner can have no trademark significance in distinguishing anyone's goods.

VI

"BARRISTER BOND" IS NOT A VALID TRADEMARK NOR IS IT OWNED BY OR HELD IN TRUST FOR H. A. FRIEND AND COMPANY

If anyone was ever in a position to exclude anyone else from use of "Barrister Bond", it was Gilbert Paper Company, the owner of Registration No. 274, 875 (Exh. 2), and not H. A. Friend and Company. The invoice agreement (Exh. I) by which Gilbert in February 1949 granted Friend Paper Company an exclusive right to the "Barrister" mark in consideration of the $400 payment, prevented even Gilbert from excluding Friend

Paper Company from using "Barrister Bond." There is no evidence that Gilbert ever held the registration in trust for H. A. Friend and Company or that Gilbert ever assigned it to H. A. Friend and Company or of the recording of any particular assignment. There is no document of any kind in the case even purporting to convey to H. A. Friend and Company any right to prevent, or recover for, alleged infringements occurring prior to August 26, 1965, which is subsequent to the filing of the Complaint in No. 22489.

The Court's Memorandum of Decision holds (Ct 472):

> "The plaintiff has been using the trademark 'Barrister Bond', ever since prior to 1926. Trademark registration No. 274,875 was issued to Gilbert in 1930 and was renewed for 20 years ...."

H. A. Friend and Company's mere <u>use</u> commencing sometime prior to 1930 is not tantamount to <u>ownership</u>, that is, the exclusive right of use; and the very fact that Gilbert obtained the registration in 1930 is evidence that it was not being held in trust for anyone else. If H. A. Friend and Company held the exclusive right to use "Barrister Bond" in 1930, Gilbert could not have validly registered it for itself. The very application to register in 1930 contained the required affidavit that no one other than Gilbert has the right to use the mark (File wrapper, Exh. E, Rt 335). Again, when Gilbert applied to republish the mark under Lanham Act Sec. 12(c) by its affidavit of July 8, 1947 (p. 7, Exh. E), the Patent Office refused to republish (Exh. E, pp. 10 and 11)

because title appeared in Southworth Company. It was not until after September 30, 1948 when Gilbert's attorney sent to the Patent Office for recording an assignment of it from Southworth to Gilbert, dated December 26, 1930, that the Patent Office republished the registration to Gilbert (pp. 7-32 of Exh. E). All this documentation shows that Gilbert was continuously claiming exclusive rights and ownership in itself in the "Barrister Bond" mark.

Since trademarks can only represent origin of goods, it is beyond legal comprehension that a trademark owner can hold a trademark "in trust" for someone else, for if such a "trust" could exist it would imply that the purported trustor has the exclusive right to use the mark; which would negate owner (Gilbert Paper Company) having even a right of use. H. A. Friend and Company could never have been a "related company" under Lanham Act Sec. 5 (15 USC 1055) because a related company can only be one which is owned or controlled by the registrant, or which controls the registrant, such as subsidiary, affiliated, and parent companies, and legitimate licensees bound by license agreements to maintain the quality of trademarked goods manufactured by them under rigid supervision by the trademark registrant. Mere customers of Gilbert's distributors cannot be "related companies" because the registrant does not control them in any way. Gilbert's customers for "Barrister Bond" are merchants such as Moser Paper Company (PreTrial Conf. Order, par. 31 and 32, Ct 452), Friend Paper Company, and a host of

others; but not retailers.

There is no evidence supporting the finding of a "trust." Mr. Schmerein, Gilbert's president, did not testify that Gilbert ever held the Barrister Bond mark in trust for anyone. The farthest Gilbert ever went in that direction (Schmerein dep. Exh. BK, p. 2) was to try to arrange that H. A. Friend and Company would be the retailer in Illinois and states contiguous thereto. As clearly stated in Gilbert's letter of October 7, 1948, to H. A. Friend (p. 2 of Exh. M): "All we did was to offer their use to you," and "you were given the use of those marks in Illinois and all of the states contiguous to Illinois."

Mr. Schmerein's testimony (Exh. BK) was that Friend Paper Company and not H. A. Friend and Company, was Gilbert's customer, and Gilbert shipped the paper to Friend Paper Company and "past that I have no reason to question what happened to it," (dept. p. 46, Exh. BK); that Friend Paper Company became the owner of the paper without any restriction from Gilbert other than the fact that if Friend Paper Company "disturbed any Gilbert franchise business," Gilbert could eliminate its future business (dep. pp. 34, 35); that Gilbert had similarly sold to Moser Paper Company without restriction and Moser could sell the paper, including "Barrister Bond", to anyone (dep. p. 35).

Mr. Schmerein admitted that Gilbert had received Friend Paper Company's letter of August 19, 1948 (p. 2 of Exh. S) (Schmerein dep. pp. 40 and 41), signed as Friend Paper Company by Wilber Friend, which stated, "this firm is solely owned and

controlled by the undersigned, W. H. Friend," and this knowledge of Gilbert is further confirmed by Gilbert's letter signed by Mr. Schmerein, dated October 1, 1948 (p. 1 of Exh. M) to H. A. Friend which contains the statement, "Due to the presence of these same watermarks with the Friend Paper Company it would be our distinct preference to see a continuance of purchases through this source."

Mr. Schmerein knew at least as early as May 1958 that Friend Paper Company was calling its paper "Barrister Bond" even though Gilbert was watermarking it as "Bar-Bond," as Schmerein admitted that Gilbert had received Friend Paper Company's letter dated May 26, 1958 carrying the notation on the bottom of the letterhead "Engraved Barrister Bond, 100% New Cotton Fiber" (Schmerein dep. pp. 44, 45) and that Gilbert had never objected to it, and that Friend Paper Company had never made any misrepresentation or committed any fraud against Gilbert (dep. pp. 55, 56).

Another reason why the "Barrister Bond" mark could not have been transferred from Gilbert to H. A. Friend and Company in the nebulous manner suggested, is that a registered mark can only be assigned by an instrument in writing together with the goodwill of the business of the assignor. (Lanham Act Sec. 10 (15 USC 1060) (Appendix II). Under this Lanham Act Sec. 10, even the written invoice agreement (Exh. I) for which Friend Paper Company paid $400 to Gilbert, was probably not an assignment of exclusive right in the registration, inasmuch as the

goodwill of Gilbert's business did not go with it and under the authorities, may have had the effect of voiding the trademark, as it amounted to a simple license. But at least Friend Paper Company was a "purchaser for a valuable consideration" of the right to buy "Barrister Bond" from Gilbert.

It is abundantly clear that Harley Friend in 1949 knew that Gilbert was the owner of "Barrister Bond," as well as the fact that all the other watermarks here in controversy were open to use by Wilber Friend, as clearly shown by the statement in Harley Friend's letter to Gilbert of April 20, 1949 (p. 2 of Exh. N); "Owing to the fact that the other three watermarks appear to be free-marks, it would only be necessary for him to get an assignment on Barrister Bond, in order to put H. A. Friend and Company completely under his thumb."

VII

H. A. FRIEND AND COMPANY DID NOT OBTAIN EVEN A PURPORTED ASSIGNMENT OF BARRISTER BOND UNTIL AFTER THE FILING OF THIS SUIT.

There is no evidence of H. A. Friend and Company's ownership of "Barrister Bond" until August 26, 1965, which is the date of the Patent Office certificate on the copy of registration 274, 875 introduced in evidence as plaintiff's Exhibit 2. This bears the Patent Office's typewritten endorsement that title is in H. A. Friend and Company. No objection was made to the hearsay aspect of this endorsement because defendants-appellants became aware

during the discovery proceedings of several mesne assignments of the registration during the 1960's by which the ownership was transferred among a number of different corporations, the last one of which executed what purports to be an assignment to H. A. Friend and Company, at a date prior to August 26, 1967 and after the commencement of this suit. Plaintiff-appellee did not see fit to introduce any of these assignments in evidence. As far as the present record is concerned, plaintiff-appellee has not shown that it has acquired anything purporting to evidence its ownership, prior to August 26, 1965.

It is clear that Gilbert is estopped by reason of the invoice agreement (Exh. I) and its lack of objection to Friend Paper Company's use of "Barrister Bond from preventing the continued use of "Barrister Bond." It should be equally clear that even if H. A. Friend and Company claims to have at this date an assignment of it, it is likewise estopped because it can be in no better position than Gilbert.

VIII

FRIEND AND COMPANY COMMENCED AND BUILT UP ITS BUSINESS IN A GEOGRAPHICAL AREA SUBSTANTIALLY SEPARATE FROM THAT OF H. A. FRIEND AND COMPANY, INC. AND ITS PREDECESSOR.

The conduct of the parties shows that when Wilber Friend moved to Pasadena both he and Harley Friend considered he had left the territory of his father's interest. Harley's silence when

told by Wilber in 1948 of Wilber's intention to go into the retail business and to use the name Friend and Company; and the absence of any reaction when Howard Friend saw the name "Friend and Company" at 55 West Green Street, Pasadena in 1956; and Harley's ignoring the information he had received from the Lycette firm in 1957 of "Friend and Company" in Pasadena and selling at retail; and plaintiff's ignoring Friend Paper Company's listings of all the trademarks in Lockwood's Directories throughout all the years coupled with their knowledge as early as 1949 that Wilber Friend had been publishing his marks in Lockwood's; all add up to the plaintiff having considered Wilber Friend to be in a different geographical area, at least up until the time when the three Friend brothers in Zion adopted a different position in 1964.

Even if Wilber Friend might have been stopped years ago from using Friend and Company in the far west states because of H. A. Friend and Company having previously done at least some business there, their lack of timely action should make the authorities on geographical separation of the parties, controlling in this case. Hanover Star Milling Co. v. Metcalf, 240 U.S. 403, 60 L.Ed. 713, 36 S.Ct. 357 (1916); United Drug Co. v. Theodor Rectanus Co., 248 U.S. 90, 63 L.Ed. 141, 39 S.Ct. 48 (1918); Silver Swan Liquor Corp. v. Hiram Walker, Inc., 19 F.Supp 445 (ND Calif. 1937); Gallo v. Safeway Brake Shops of La., Inc., 140 So. 2nd 912, 915 (La.App., 1963), quoting 87 CJS 235 (Appendix II).

IX

LACHES, ACQUIESCENCE AND ESTOPPEL ARE A BAR TO THE FIRST SUIT.

All findings and judgments of the District Court are under the Lanham Act and they should not be maintained because of the equitable defense of laches, and also the defenses of acquiescence and estoppel, all of which are specifically preserved in Lanham Act Sec. 19 (USC 1069) (Appendix II). These defenses, all of which are in defendants' Answer, are established by the long delay of over 16 years in bringing the action after the matters complained of were commenced, during all of which time the plaintiff was alerted and on notice of defendants' activities and intentions and knew of them and recognized, acquiesced and made no objection to defendants' use of any of the names or marks Friend Paper Company, Friend and Company, Friends, Banner, and Barrister. This situation also results in an estoppel against the plaintiff by reason of defendants-appellants' having spent large amounts of money, time and effort over the years building up their business and plant in Pasadena in reliance on plaintiff's acquiescence and lack of objection.

The concession of the right to continue use of the name Friend Paper Company, at least after 1948, should now bar any injunction against its use. It follows that defendants should not be enjoined from using the word Friend or Friends in connection with their business and products; for the right to use the name

Friend Paper Company for a stationery business must include the right to refer to the products as Friend or Friend's paper, especially when the proprietor of the business is named Friend.

Considering furthermore that products sold by Friend Paper Company even prior to 1949 had been marked and referred to as Friend, Friends, Barrister, Barrister Bond, Banner, and Banner Bond, plaintiff's recognition that Friend Paper Company was entitled to continue its business as before 1949 carries with it the right to continue to handle and sell Friend, Friends, Barrister and Banner, as before.

Furthermore, customers of Friend Paper Company, including Friend and Company, are entitled to sell the products bearing these marks; otherwise the right of Friend Paper Company to handle these lines would be meaningless.

ESTOPPEL

Even if there were no laches or acquiescence involved, the plaintiff is nevertheless estopped to maintain this action by reason of its actions and conduct which lulled the defendants into a sense of security on which they relied in building up their plant and business. Plaintiff should not be permitted to stand idly by and watch the plant and business of defendant Friend and Company build up until it reached its present large proportion and then come into court with an action calculated to cripple it and take over the goodwill generated by that defendant in the western states.

The Memorandum of Decision in holding an absence of

laches (Ct 476, 477) considered only one of the many incidents referred to as showing H. A. Friend and Company being alerted and knowing of the activities complained of, namely, the letter from the Lycette law firm in Seattle dated April 3, 1957 to which Harley Friend replied on April 5, 1957 (Exh. AF, AG). This should have been enough. The present suit was not filed until more than 7 years later, on June 17, 1964. This Court has held in Whitman v. Walt Disney Products, Inc., 263 F.2d 229, 120 USPQ 253 (9 Cir., 1958) that any delay of more than 6 years in bringing suit after having knowledge of the facts complained of, is presumed to be laches.

The reason given by the District Court for rejecting the defense of laches in the present case is in the sentences (Ct 476), "However, he took no action with respect to the matter prior to his death two years later, nor did he inform his other sons, who were his partners, concerning it .... In any event, the first knowledge that Richard, Howard or William had was in August 1962."

William's testimony was that his father had taken the letter without telling any of his sons, and answered it. Even assuming that William Friend's testimony is factually correct, the court's conclusion that H. A. Friend and Company had not been put on notice of Wilber Friend's Pasadena business named Friend and Company, as early as April 1957, is erroneous as a matter of law. Receipt of notice by any firm member is sufficient to charge the firm with notice. 68 CJS 572 (Partnership Sec. 137); In re Fineberg, 36 F.2d 392 (WD NY, 1929); Stork Restaurant Inc. v. Sahati,

166 F. 2d 348, 362 (9 Cir., 1948). (Appendix II).

The District Court decision was silent in respect to all of the other incidents and events showing that H. A. Friend and Company had been alerted even much earlier than 1957. These include (1) the visit of Howard Friend to the office of Friend and Company in 1956, (2) the public advertising of Friend Paper Company in Lockwood's Directory continuously since 1948 of its paper marked "Barrister Bond," "Friends" and "Banner Bond," (3) Harley Friend's expression in his letter of April 20, 1949 (Exh. N) that he knew of Friend Paper Company's intention to use all of the marks involved in this suit and that H. A. Friend and Company did not have exclusive rights to any of them as they were all "free-marks" excepting "Barrister Bond" which only Gilbert could control, (4) the testimony of Wilber Friend that he had visited the members of his family who are members of H. A. Friend and Company, a number of times throughout the 1950's and had given one or more of his brothers his business card bearing the name Friend and Company, (5) the fact that Wilber Friend's son and daughter had both worked at times during the 1950's at H. A. Friend and Company in Zion.

The Decision of the District Court did not give any consideration to the factor of estoppel, urged by defendants-appellants, arising from the fact that the defendants had started business in California from nothing and had built it up to a substantial amount with heavy expenditures in reliance on the acquiescence (except for Barrister Bond) of Harley Friend in the use of the trade names

and trademarks involved.

Richard, Howard and William Friend, by the present action, are attempting to upset what their father had settled and decided in 1949 and did not see fit to disturb in 1957.

Menendez v. Holt, 128 U.S. 514, 32 L.Ed. 526, 9 S.Ct. 143 (1888) states the general proposition that bare laches alone, while constituting a bar to the recovery of damages and profits, will not ordinarily bar an injunction, but also points out that an injunction can be barred by long acquiescence or extenuating circumstances such as estoppel or inequity. W. A. Gaines & Co. v. Rock Spring Distilling Co., 226 F. 531 (C.A. 6, 1915); Landers, Frary and Clark v. Universal Cooler Corp. et al, 85 F.2d 46, 30 USPQ 248 (C.A. 2, 1936); Anheuser Busch Inc. v. DuBois Brewing Co., 175 F.2d 370, 81 USPQ 423 (C.A. 3, 1949).

X

REGISTRATION NOS. 655,848 AND 544,450 FOR "FRIENDS" AND "FRIENDS LINEN" RESPECTIVELY, AND NO. 274,875 FOR "BARRISTER BOND" SHOULD BE CANCELLED.

Defendants-appellants counterclaim for cancellation of Registration No. 655,848, 544,450 and 274,875, under the provision of Lanham Act Sec. 37 (15 USC 1119) (Appendix II). If defendants-appellants have the right to use "Friends" and "Barrister," and their trade names Friend Paper Company and Friend and Company, as they contend above, they are damaged by the registrations which should therefore be cancelled.

XI

DEFENDANTS-APPELLANTS ARE ENTITLED TO A DECLARATION OF THEIR RIGHT TO CARRY ON THEIR BUSINESSES.

In the light of the arguments and facts set forth hereinabove, defendants-appellants should be entitled to a declaration that they are free to carry on their businesses as previously, under their respective names Friend Paper Company and Friend and Company, and under the marks "Barrister," "Banner," "Friend" and "Friends."

XII

CIVIL ACTION NO. 66-470-WPG, APPEAL NO. 22489A, SHOULD BE DISMISSED FOR LACK OF JURISDICTION AND FOR FAILURE TO STATE A CLAIM FOR WHICH RELIEF MAY BE GRANTED.

In respect to this action, the District Court's Memorandum of Decision states (Ct 475):

> "The plaintiff is entitled to, and will be accorded, an injunction against further misrepresentations by the defendants concerning the quality of their merchandise. See Chamberlain v. Columbia Pictures Corp., 186 F.2d 923, 924 (9 Cir. 1951)."

On or about June 9, 1966 defendants-appellants presented their Motion to Dismiss this action on the above-captioned grounds (Ct 253), citing Chamberlain v. Columbia Pictures Corp., supra, which motion was denied by the Court in an order entered on or about August 7, 1966, but without prejudice to the right of defendants

to renew the motion during the trial and maintain the defense, which defendants did.

The Court's ruling was based on 15 USC 1125(a) (Appendix II) (Ct 474), which has held not to cover false description or false advertising or sale of inferior products.

The leading case in the 9th Circuit is Chamberlain v. Columbia Pictures Corp., 186 F. 2d 923, 89 USPQ 7 (1951) in which the defendant therein sought to produce a movie falsely advertising it as originating with Mark Twain, whose heir brought the action under 15 USC 1125(a) for false advertising. This Court said, at 186 F. 2d 923, 925, 89 USPQ 7, 9,

> "At first blush it might be said that the allegations made fit snugly into the provisions of §1125, Title 15 USCA. However, we do not think said section changes the fundamental requirements necessary to sustain a suit for unfair competition, one such requirement being a direct injury to the property rights of a complainant by passing off the particular goods or services misrepresented as those of complainant. Deceiving the public by fraudulent means, while an important factor in such a suit, does not give the right of action unless it results from the sale of the goods as those of the complainant."

The Massachusetts District Court in arriving at a similar result in Sampson Crane Co. v. Union National Sales, Inc., 87 F. Supp 218, 83 USPQ 507 (DC Mass. 1949) affirmed 180 F. 2d 896, 96 USPQ 454 (1st Cir. 1950), said at 87 F. Supp 218, 222 that the

section must be limited "to that 'unfair competition' which has been most associated with the misuse of trademarks, i.e., the passing off of one's own goods as those of a competitor."

Although the Complaint alleges passing off the alleged low grade envelopes and paper as the product of the plaintiff, the basic cause of action in this case is the sale of inferior goods, which cannot be made into a passing off type case simply by using the words "passed off."

There is not any evidence nor even any allegation that the alleged misrepresentations of fiber content relate in any way to misrepresenting defendants' products as those of the plaintiff. Whatever passing off could be involved on these appeals is involved in the first case, Civil Action 64-805-WPG which alleges likelihood of confusion based on defendants' use of their name and trademarks.

It should be noted here that the 3rd Circuit and the District of Columbia in the cases of L'Aiglon Apparel, Inc. v. Lana Lobelle, Inc., 214 F. 2d 649 (3 CCA, 1954) and Gold Seal Co. v. Weeks, 129 F. Supp 928 (DC DC, 1955), affirmed 230 F. 2d 832, cert. denied, 352 U.S. 829, appear to disagree with the 9th Circuit and the 1st Circuit in respect to the scope of 15 USC 1125(a).

Glenn v. Advertising Publications, Inc., 251 F. Supp. 889, 148 U. S. P. Q. 645 (SD NY, 1966) and General Pool Corp. v. Hallmark Pool Corp., 259 F. Supp. 383, 151 U. S. P. Q. 372 (ND Ill,, 1966) appear to agree with the 1st and 9th Circuit holdings in Chamberlain and Sampson Crane, supra.

XIII

THERE SHOULD BE NO AWARD OF ANY DAMAGES TO THE PLAINTIFF NOR OF ANY OF THE DEFENDANTS' PROFITS.

If defendants-appellants prevail in their appeals there should be no monetary assessments against them. The following discussion is on the contingency they do not prevail.

The District Court found that the "acts of trademark infringement on the part of the defendants resulted in actual damages to the plaintiff" in the sum of $5, 000, which it trebled under 15 U. S. C. 117 to the sum of $15, 000. In arriving at the amount of $5, 000 actual damages, the Court said (Ct 477):

> "Most of the sales thereby lost by the plaintiff to the defendants quite apparently were small in dollar amount; and to seek to identify each of them through an accounting would be releatively expensive and basically impractable. However, the court interpolates and finds from the evidence presented that the plaintiff's actual damages in the respects here under consideration are at least the sum of $5, 000."

There is no indication of how the $5, 000 was reached, nor the nature of the interpolation. The sales chart, Exh. AK, does not indicate any damage, that is, lost sales to the plaintiff, as there was a slight rise in its western state sales from the 1940's to the 1950's.

Damages cannot be arrived at arbitrarily, and the finding that even an accounting would be basically impractical indicates that the $5, 000 could not even be a probable estimate. The measure of recovery of damage is not what the defendant has gained but what the plaintiff has lost, that is, lost profits to the plaintiff, and they must be shown by sufficient evidence. Coupe v. Royer, 155 U.S. 565, 581, 39 L.Ed. 263, 269 (1894); Aro Mfg. Co. v. Convertible Top Replacement Co., 377 U.S. 476, 507, 12 L.Ed. 2d 457, 480; Harley and Lund Corp. v. Murray Rubber Co., 31 F.2d 932, 933 (2nd Cir. 1929), cert. denied 279 U.S. 872, 73 L.Ed. 1007 (1929).

The District Court correctly refrained from awarding any profits of the defendants for the reason that no profits of defendants are in evidence and furthermore there is no evidence that any profits of defendants are due to the alleged infringements. There is no evidence that the 3, 500 customers of Friend and Company including 500 in California (Rt 432) bought their goods because of any trademarks of H. A. Friend and Company. Where goods bearing an infringing trademark are sold for profit, and the purchasers bought the goods because of the infringer's recommendation or his reputation or any other reason than response to the

appeal of the trademark owner's symbol, the trademark owner is not entitled to the infringer's profits. Mishawaka Rubber and Woollen Mfg. Co. v. S. S. Kresge Co., 316 U.S. 203, 86 L.Ed. 1381 (1942), rehearing denied 316 U.S. 712, 86 L.Ed. 1777.

The Lanham Trademark Act Sec. 35, 15 U.S.C. 1117, does not allow the infringer's profits except to the "registrant of a mark registered in the Patent Office". The only registration in suit owned by the plaintiff is the "Friends" registration No. 655,848. The plaintiff, never having had even colorable title to the "Barrister Bond" registration until the latter part of 1965, after the filing of the suit, does not even have a cause of action on that. There is no showing of any particular amount of profit made by defendants on account of any alleged infringement of the "Friends" registration.

Lanham Act Sec. 35 does not require the court to assess any profits or damages at all, but only "subject to the principles of equity"; and also any assessment is subject to the provisions of Secs. 29 and 32. Sec. 29 (15 U.S.C. 1111) (Appendix II) provides that no damages or profits are recoverable unless the plaintiff displayed with his mark as used a notation to the effect that it was registered in the U. S. Patent Office, or else that the defendant had actual notice of the registration (15 U.S.C. 1111). There is no evidence of any such notice of any marks as used in plaintiff's goods, or that defendants had any actual knowledge of the "Friends" registration until plaintiff filed its suit, nor that plaintiff even purported to own the "Barrister Bond" registration,

until long after the filing of the suit.

It is submitted that the actual damages found by the court should not have been trebled to $15,000 for the reason that the defendants had ample reason for believing that they had a right to use all the marks and trade names in suit, for the reasons discussed hereinabove. Trebling damages would greatly exaggerate the magnitude of the relatively few instances where customers were deceived by the reference to "Western Division", "Zion", "1908" and the map.

The Memorandum of Decision holds that the misrepresentations of cotton fiber content resulted in damage under 15 U.S.C. 1125(a) of not less than $20,000, for which judgment was given (Ct 477, 478), but no basis for that or any other figure is stated, and it appears to be an arbitrary figure. The finding of the court was that (Ct 475) "of much greater concern to the plaintiff from the standpoint of damage, is the likelihood that in future years people who have bought stationery from the defendants will become aware of the pool quality and will quietly determine never again to purchase "Friends' papers". This apparently refers to the testimony of Gilbert's officer noted in the Decision (Ct 474) to the effect that 100% cotton fiber lasts 100 years, 50%, 50 years and 25%, 25 years. Thus there would be a wait of 25 years before any such awareness would occur - and only a minor part of defendants' paper is of the 25% grade. Only a minor part of defendants' products were the subject of any errors in advertising. Much of the error occurred in respect to envelopes, which are thrown

away immediately on receipt by the addressee, and do not have time to deteriorate.

The Court further held (Ct 475) that "it is impossible to determine the full extent to which the false descriptions herein concerned have damaged the plaintiff already and will cause further injury in the future". It is submitted that the damage found by the Court is without sufficient foundation and is too speculative and should be reversed.

There is no evidence of any damage or even of any sales lost by plaintiff on account of the alleged misrepresentations. Of the approximately 26,000 lawyers in California (Exh. AR) appellee has about 15 of them and appellant has about 425-450 of them. There is no reason for supposing that any customers which Friend and Company might have obtained by a low price made possible by "inferior goods" would have gone to appellee if the goods were not "inferior".

XIV

NO ATTORNEY'S FEES SHOULD BE AWARDED TO PLAINTIFF-APPELLEE.

The District Court awarded $30,000 attorneys' fees (Ct 478) citing National Van Lines v. Dean, 237 F.2d 688 (9 Cir. 1956). However, the later case of Maier Brewing Co. v. Fleischmann Distilling Corp., 359 F.2d 156, 149 U.S.P.Q. 89 (9 CCA, 1966), affirmed by the Supreme Court in Fleischmann Distilling Corp.

v. Maier Brewing Co., 386 U.S. 714, 18 L. Ed. 2d 475, 87 S. Ct. 1404, leaves no basis in National Van Lines v. Dean for awarding any attorney's fees, as the Supreme Court has affirmed that attorney's fees cannot be awarded in Lanham Act cases even when there is deliberate infringement. Both of the present actions and the judgment of the District Court are based on the Lanham Act.

Where, as here, the district court does not set forth the basis on which the attorney's fees are awarded, the award should be set aside. Dubil v. Rayford, Camp & Co., 184 F. 2d 899, 902 (9 CCA, 1950); Speed Corp. v. Webster, 262 F. 2d 482 (9 CCA, 1959).

Furthermore, appellants had good reason for believing they had meritorious defenses, hence attorney's fees should not be awarded in any event. Park-In Theatres v. Perkins, 190 F. 2d 137, 142,90 U.S.P.Q. 163, 167 (9 CCA, 1951).

XV

DEFENDANTS-APPELLANTS SHOULD NOT BE ENJOINED FROM USING "BAR-BOND."

The Court's injunction on "Bar-Bond" was based on Wilber Friend's mental attitude that Bar is an abbreviation of "Barrister." The real question is, however, the customer's mental attitude, for the issue is likelihood of confusion of the customer. It is submitted that "Bar" is not likely to be confused with "Barrister."

XVI

THERE SHOULD BE NO INJUNCTION AGAINST USE OF "FRIEND," "FRIENDS," "BANNER," "BARRISTER BOND" OR "FRIEND AND COMPANY."

If defendants-appellants prevail in their defenses and arguments herein, then there should be no such injunction.

XVII

DEFENDANTS-APPELLANTS SHOULD NOT BE ENJOINED FROM OPPOSING THE APPLICATION TO REGISTER "BANNER."

An Opposition in the Patent Office is a well-known and frequently used proceeding to protect an Opposer and the public from improper issuance of trademark registrations, and appellants should not be prevented from exercising their right to oppose.

XVIII

DEFENDANTS-APPELLANTS SHOULD NOT BE ENJOINED FROM USE OF "FRIEND PAPER COMPANY" OUTSIDE THE WHOLESALE BUSINESS.

Plaintiff's acquiescence in the name Friend Paper Company, effected through the silence of Harley Friend when told about it in 1948, should not be construed as imposing limitations on the scope of its business. Harley's silence could not indicate to Wilber that there was any such limitation on the acquiescence. The limitation to the wholesale business represents appellee's present wish, but not the understanding of Harley and Wilber Friend in 1948.

XIX

DEFENDANTS-APPELLANTS SHOULD NOT BE ENJOINED FROM ASSERTING THEIR BUSINESS BEGAN PRIOR TO 1950 OR HAS RELATIONSHIP WITH ZION OR THAT THE PASADENA ESTABLISHMENT IS THE DIVISION OF ANY COMPANY.

Friend Paper Company was Wilber Friend's sole proprietorship in 1949, and if appellants' argument prevails, as early as the 1930's. In the same period, it had its post office address in Zion without objection from appellee, hence should be entitled to continue it for business purposes. If it be held that appellants are entitled to continue to use "Friend and Company", it cannot harm the appellee to state that it is a division of Friend Paper Company. If the injunction against use of the name Friend and Company is affirmed, then a reference that its new company name is a division of Friend Paper Company or of some other company cannot affect appellee. No injunction should be so broad as to prevent appellants from opening a business office and address in Zion if they should wish, as they had done in 1949 and earlier.

XX

DEFENDANTS-APPELLANTS SHOULD NOT BE ENJOINED FROM SELLING STATIONERY OF DIFFERENT QUALITY FROM ADVERTISED.

Appellants have already corrected all known errors in their catalogs and do not intend to resume them; hence the injunction is not important. However, as a legal point, there should be

no injunction without a valid cause of action, and for the reasons argued herein, Lanham Act Sec. 43(a) (15 U.S.C. 1125[a]) did not give the appellee any cause of action.

XXI

FINDINGS OF FACT OF THE DISTRICT COURT ARE ERRONEOUS.

The erroneous findings of the District Court appear at various places in its Memorandum of Decision and without formal numbering. The errors have been pointed out hereinabove under pertinent captions.

CONCLUSION

It is respectfully submitted that this Court should find:

1. That the Complaints should be dismissed and the injunctions vacated.

2. That defendants-appellants have the unrestricted right to use "Friend", "Friends", "Friend Paper Company", "Friend and Company", "Barrister" and "Banner", and the like, in connection with their stationery products and their business.

3. That the "Friends" and "Barrister Bond" trademarks and registration Nos. 655,848 and 274,875 are invalid, and that these registrations and also the "Friends Linen" registration No. 544,450 should be cancelled.

4. That the plaintiff-appellee's suit be held barred by laches, acquiescence and estoppel.

5. That no monetary award or attorney's fees be granted to plaintiff-appellee.

6. That the District Court's Findings of Fact and Conclusions of Law, referred to in the Assignment of Errors herein, are in error, and that the portion of the judgment of the District Court holding the alleged trademarks of appellee valid, should be reversed, as should that portion awarding monetary recovery and attorney's fees to appellee.

DATED: At Pasadena, California
June 12, 1968.

Respectfully submitted,

ANGUS & MON

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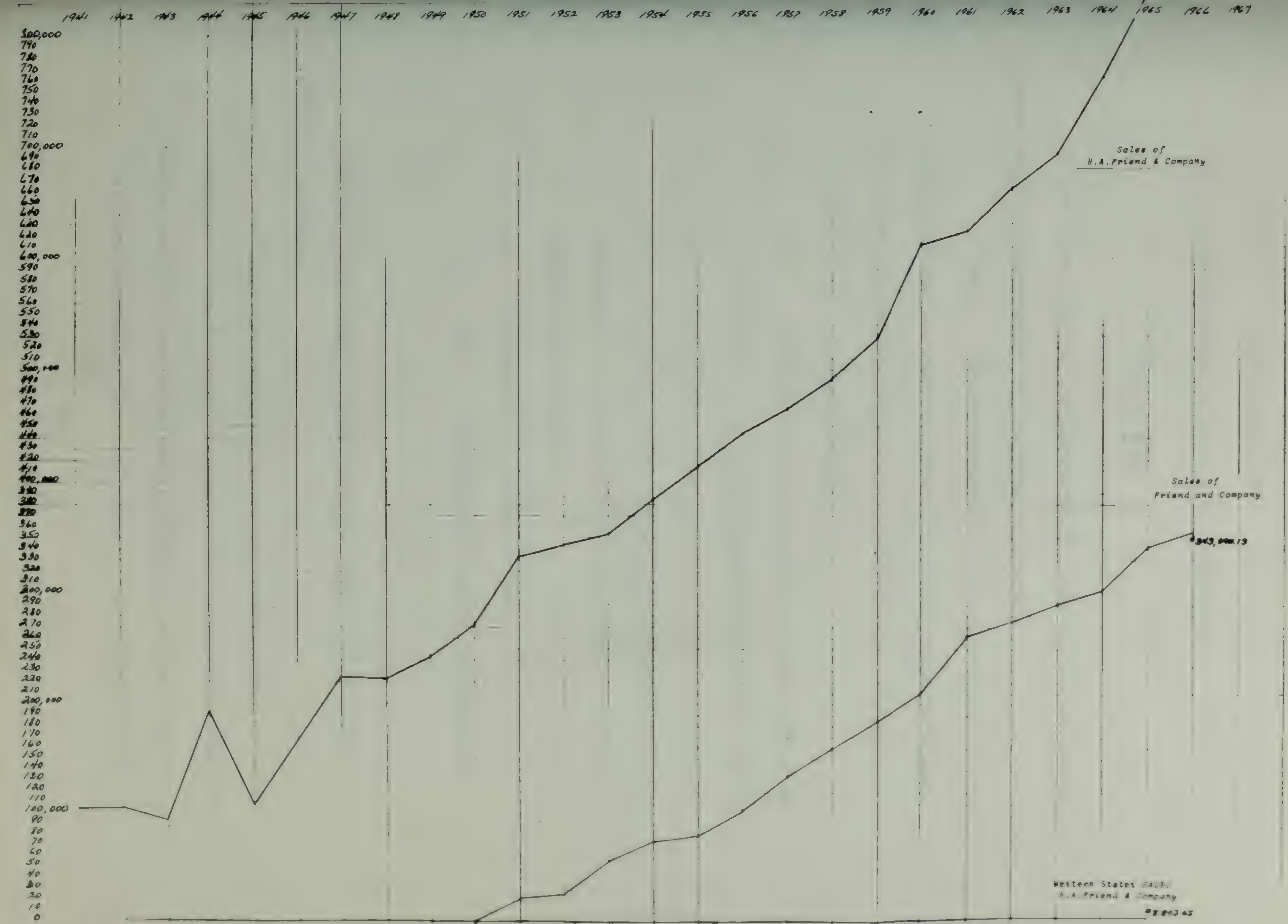
Attorneys for Defendants-Appellants.

<u>CERTIFICATE</u>

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ D. Gordon Angus
D. GORDON ANGUS



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APPENDIX II

Pertinent Statutes, Cases and Authorities

STATUTES

A pertinent part of the Lanham Act Sec. 2 (15 USC 1052), governing the registration of trademarks reads:

> "Sec. 2. No trademark by which the goods of the applicant may be distinguished from the goods of others shall be refused registration on the Principal Register on account of its nature unless it ....
>
> (d) Consists of or comprises a mark which so resembles a ..... trade name previously used in the United States by another and not abandoned, as to be likely, when applied to the goods of the applicant, to cause confusion or mistake or to deceive purchasers ....
>
> (e) Consists of a mark which .....
>
> (3) is primarily merely a surname."

The pertinent part of Lanham Act, Sec. 8(a) (15 USC 1058[a]) provides:

> "That the registration of any mark under the provisions of this Act shall be cancelled by the Commissioner at the end of 6 years following its date, unless within 1 year next preceding the expiration of such 6 years the

registrant shall file in the Patent Office an affidavit showing that said mark is still in use . . . ."

Lanham Act, Sec. 10 (15 USC 1060) provides:

"A registered mark or a mark for which application to register has been filed shall be assignable with the goodwill of the business in which the mark is used, or with that part of the goodwill of the business connected with the use of and symbolized by the mark, ... Assignments shall be by instruments in writing duly executed . . . . . An assignment shall be void as against any subsequent purchaser for a valuable consideration without notice, unless it is recorded in the Patent Office within three months after the date thereof or prior to such subsequent purchase."

Lanham Act, Sec. 14 (15 USC 1064) provides:

"Any person who believes that he is or will be damaged by the registration of a mark on the principal register . . . . . may [apply] to cancel said registration . . . .

(c) At any time if the registered mark . . . . . has been abandoned, or its registration was obtained fraudulently . . . ."

Lanham Act, Sec. 15 (15 USC 1065) provides:

> "Except on a ground for which application to cancel may be filed at any time under subsections (c) and (e) of section 14 of this Act, ... the right of the registrant to use such registered mark in commerce ..... shall be incontestable: Provided that: .....
>
> (3) an affidavit is filed ..... setting forth ..... [that] such mark has been in continuous use for ..... [the preceding] 5 consecutive years ...."

Lanham Act, Sec. 19 (15 USC 1069) provides:

> "In all inter partes proceedings equitable principles of laches, estoppel and acquiescence, where applicable, may be considered and applied."

Lanham Act, Sec. 33(b) (15 USC 1115[b]) provides:

> "If the right to use the registered mark has become incontestable under section 15 hereof, the registration shall be conclusive evidence of the registrant's exclusive right to use the registered mark in commerce on or in connection with the goods or services specified in the affidavit filed under the provisions of said section 15 subject to any conditions or limitations stated therein except when one of the following defenses or defects is established:

(1) That the registration or the incontestable right to use the mark was obtained fraudulently; or

(2) That the mark has been abandoned by the registrant; or

(3) That the registered mark is being used, by or with the permission of the registrant or a person in privity with the registrant, so as to misrepresent the source of the goods or services in connection with which the mark is used; or

(4) That the use of the name, term, or device charged to be an infringement is a use, otherwise than as a trade or service mark, of the party's individual name in his own business, or of the individual name of anyone in privity with such party, or of a term or device which is descriptive of and used fairly and in good faith only to describe to users the goods or services of such party, or their geographical origin; or

(5) That the mark whose use by a party is charged as an infringement was adopted without knowledge of the registrant's prior use and has been continuously used by such party or those in privity with him from a date prior to registration of the mark under this Act or publication of the registered mark under subsection (c) of section 12

of this Act; Provided, however, That this defense or defect shall apply only for the area in which such continuous use is proved; or

(6) That the mark whose use is charged as an infringement was registered and used prior to the registration under this Act or publication under subsection (c) of section 12 of this Act of the registered mark of the registrant, and not abandoned; Provided, however, That this defense or defect shall apply only for the area in which the mark was used prior to such registration or such publication of the registrant's mark; or

(7) That the mark has been or is being used to violate the antitrust laws of the United States."

Lanham Act, Sec. 37 (15 USC 1119) reads:

"In any action involving a registered mark the court may determine the right to registration, order the cancelation of registrations, in whole or in part, restore canceled registrations, and otherwise rectify the register with respect to the registrations of any party to the action. Decrees and orders shall be certified by the court to the Commissioner, who shall make appropriate entry upon the records of the Patent Office, and shall be controlled thereby."

Lanham Act, Sec. 43(a) (15 USC 1125[a]) provides:

"Any person who shall affix, apply, or annex, or use in connection with any goods or services, or any container or containers for goods, a false designation of origin, or any false description or representation, including words or other symbols tending falsely to describe or represent the same, and shall cause such goods or services to enter into commerce, and any person who shall with knowledge of the falsity of such designation of origin or description or representation cause or procure the same to be transported or used in commerce or deliver the same to any carrier to be transported or used, shall be liable to a civil action by any person doing business in the locality falsely indicated as that of origin or the region in which said locality is situated, or by any person who believes that he is or is likely to be damaged by the use of any such false description or representation."

EXCERPTS FROM CASES
(Alphabetically Arranged)

In Academy of Motion Picture Arts and Sciences v. Benson, 15 C. 2d 685, 690 (1940), the court, quoting 63 Corpus Juris 394 (now 87 CJS, 321-322) stated:

"If plaintiff proves that the name or word has been so exclusively identified with his goods or business

as to have acquired a secondary meaning, so as to indicate his goods or business and his alone, he is entitled to relief against another's deceptive use of such items, but if he fails in such proof he is not entitled to relief . . . ."

In Gallo v. Safeway Brake Shops of La., Inc., 140 So. 2d 915 (La. App. 1962), the court said in quoting 87 CJS 235:

"Where two users of the same or similar trademark occupy essentially different territory, each is entitled to its exclusive use in his own territory as against the other, regardless of which was the earlier user . . . ."

In R. L. Bennett & Sons v. Farmers Seed and Gin Co., 288 F. 365 (CA 5, 1923), headnote 3 reads:

"Trademarks may be lost by acquiescence in their use by others, and where plaintiffs sold cotton seed of considerable value and accepted payment therefor with full knowledge and acquiescence that the seed would be used by the buyer in the cotton seed business, and the cotton grown therefrom and the cotton seed thereby produced would be advertised and sold as 'Bennett's New Cotton,' and the plaintiff assisted in the preparation of defendant's advertising matter, and advised as to new methods of ginning, plaintiffs were estopped from con-

tending that the name 'Bennett's New Cotton' was an exclusive trademark, which defendants were not permitted to use."

Tomsky v. Clark, 73 CA 412, 238 P. 520 (1925) contains the following statement:

"First, 'that by care, attention, skill and strict adherence to business.' they had built up an 'extensive and profitable' business; and secondly, that defendants, by fraudulent use of the corporate name and by unfair and fraudulent practices, were deceiving and misleading the public, and were thereby seeking to deprive plaintiffs of their customers and trade."

OTHER AUTHORITIES

In the text, Callmann on Unfair Competition and Trademarks, 2nd Edition, published 1950, Volume 3, at page 1338, the following appears:

"Sec. 79.1. Abandonment, Loss of Distinctiveness, Estoppel by Laches, Distinguished.

. . .

(1) A trademark owner may abandon his right, or more correctly, forfeit his right by abandonment. In other words, he consciously transfers or surrenders his claim to the mark by consenting to its use by others.

This we may call actual acquiescence.

(2) A trademark owner may be estopped from challenging the use of his mark by another if, because of his laches, i. e., failure to voice timely objection, the junior user developed a trademark in the belief that his use was unobjectionable. The latter may have been unaware of the trademark owner's right, or may have reasonably assumed that the trademark owner's failure to protect connoted acquiescence. This we may call 'apparent' acquiescence or acquiescence by operation of law . . . ."

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68 CJS 572 (Partnership, Sec. 137) states:

"Whatever one partner does in the course and scope of the partnership business is the act of the firm and all the partners and is binding on them, notwithstanding that it is done without the knowledge or consent of the other partners." Citing In re Fineberg, 36 F.2d 392 (WD NY, 1929).

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68 CJS 629 (Partnership, Sec. 175) states:

"Notice to, or knowledge of, an acting partner with respect to any matter relating to a transaction within the ordinary scope of the firm's business is notice or knowledge as to all the partners, including those sub-

sequently admitted to the firm" Citing Stork Restaurant, Inc. v. Sahati, 166 F.2d 348, 362 (9 Cir. 1948).

APPENDIX III

EXHIBIT	FOR IDENTIFICATION Reporter's Transcript	IN EVIDENCE Reporter's Transcript
1 to 3	7	7
4 to 7	7	
8	7	7
9	7	
10 to 15	7	7
16 and 17	7	
18	7	7
19 to 31	7	
32 (94)	7	162
33 to 49	7	
50	7	7
51 to 74	7	
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NO. 22391

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

MORRIS W. LEE,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

FILED

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APPELLEE'S BRIEF

APPEAL FROM
THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

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APPELLEE'S BRIEF

I

STATEMENT OF FACTS, STATEMENT OF PLEADINGS AND FACTS DISCLOSING JURISDICTION

On March 16, 1962 the appellant was arrested in Long Beach, California and a complaint was issued for violation of Title 18, United States Code, Section 500. On March 28, 1962 the Federal Grand Jury for the Southern District of California returned an indictment in five counts charging appellant in Counts 1 - 4 with violations of Title 18, United States Code, Section 500, in that he had passed, uttered, and published forged postal money orders [C. T. 2-6]. [1/] On April 9, 1962 appellant was arraigned

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1/ C. T. refers to pages of Court's Transcript.

and bond was reduced to $2, 500 [C. T. 7]. On April 23, 1962 defendant plead guilty to each of Counts 1 and 2 and not guilty to each of Counts 3 and 4 [C. T. 8]. The case was referred to the Probation Office for investigation and report [C. T. 8]. On May 22, 1962 the Honorable William M. Byrne, Sr., United States District Judge, sentenced appellant to five years imprisonment on each of Counts 1 and 2 to begin and run concurrently. Counts 3 and 4 were dismissed [C. T. 12 and 13]. On August 21, 1967 appellant filed a Motion for Correction of Sentence and an affidavit in forma pauperis [C. T. 14-25]. This motion was denied by the Honorable William M. Byrne, Sr., the sentencing judge, in a written order filed September 15, 1967 [C. T. 26 and 27]. On October 4, 1967 appellant filed a Notice of Appeal and Designation of Record, and Motion to Proceed in Forma Pauperis, dated September 21, 1967 [C. T. 28-33]. On October 4, 1967 Judge Byrne ordered that appellant be permitted to proceed on appeal in forma pauperis [C. T. 34].

Jurisdiction of the District Court was based on Title 18, United States Code, Sections 3231 and 500 and Rule 35 of the Federal Rules of Criminal Procedure. Jurisdiction of the court is based on Title 28, United States Code, Section 1294(1) and Rule 37(a) of the Federal Rules of Criminal Procedure.

II

PERTINENT STATUTES

Title 18, United States Code, Section 500 provides in pertinent part:

> " . . . Whoever with intent to defraud, passes, utters or publishes, any . . . forged or altered money order or postal note, knowing any material signature . . . thereon to be false, forged or counterfeited. . . ."
>
> [shall be fined not more than $5, 000 or imprisoned not more than 5 years, or both.]

Title 18, United States Code, Section 3568, as amended in 1966, provides in pertinent part:

> "The sentence of imprisonment of any person convicted of an offense shall commence to run from the date on which such person is received at the penitentiary, reformatory, or jail for service of such sentence. The Attorney General shall give any such person credit toward service of his sentence for any days spent in custody in connection with the offense or acts for which sentence was imposed. . . .
>
> "No sentence shall prescribe any other method of computing the term."

As amended June 22, 1966, Pub. L. 89-465, Section 4, 80 Stat. 217.

Prior to 1966, Section 3568, as amended in 1960, provided in pertinent part as follows:

> "The sentence of imprisonment of any person convicted of an offense in a court of the United States shall commence to run from the date on which such person is received at the penitentiary, reformatory, or jail for service of said sentence: provided, that the Attorney General shall give any such person credit toward service of his sentence for any days spent in custody prior to the imposition of sentence by the sentencing court for want of bail set for the offense under which sentence was imposed where the statute requires the imposition of a minimum mandatory sentence. . . .
>
> "No sentence shall prescribe any other method of computing the term."

As amended September 2, 1960, Pub. L. 86-691, Section 1(a), 74 Stat. 738.

Prior to the enactment of the above cited amendments, the statute provided in pertinent part:

> "The sentence of imprisonment of any person convicted of an offense in a court of the United States shall commence to run from the date on which such

person is received at the penitentiary, reformatory, or jail for service of said sentence. . . .

"No sentence shall prescribe any other method of computing the term."

June 25, 1948, c. 645, 62 Stat. 838.

III

QUESTIONS PRESENTED

A. Whether the District Court properly denied appellant's claim for credit toward service of his sentence for the time spent in custody prior to imposition of sentence.

IV

ARGUMENT

A. THE DISTRICT COURT PROPERLY DENIED APPELLANT'S CLAIM FOR CREDIT TOWARDS SERVICE OF HIS SENTENCE FOR DAYS SPENT IN CUSTODY PRIOR TO IMPOSITION OF SENTENCE.

1. UNDER THE 1960 AMENDMENT TO TITLE 18, UNITED STATES CODE, SECTION 3568, APPELLANT WAS NOT ENTITLED TO CREDIT FOR DAYS SPENT IN CUSTODY PRIOR TO IMPOSITION OF SENTENCE.

Prior to 1960, Title 18, United States Code, Section 3568,

provided that a sentence of imprisonment would commence to run from the date on which such person was received at the place of confinement for service of sentence.(June 25, 1948, c. 645, 62 Stat. 838.)

In 1960 the section was amended to require the Attorney General to credit a sentenced defendant for any days spent in custody prior to imposition of sentence for want of bail set for the offense under which sentence was imposed <u>where the statute requires the imposition of a minimum mandatory sentence</u>. (September 2, 1960, Pub. L. 86-691, Section 1(a), 74 Stat. 738, Emphasis added.) The Act was again amended in 1966 to require automatic administrative credit to all defendants sentenced after its effective date. (Title 18, United States Code, Section 3568, as amended June 22, 1966, Pub. L. 89-465, Section 4, 80 Stat. 217.)

Appellant was sentenced in 1962. He does not contend, nor does the law provide, that the 1966 amendment applies retroactively. <u>Stapf</u> v. <u>United States</u>, 367 F.2d 326, 329 (D.C. Cir. 1966). However, appellant asserts that on the authority of <u>Stapf</u>, <u>supra</u>, and <u>Dunn</u> v. <u>United States</u>, 376 F.2d 191 (4th Cir. 1967), he is entitled to administrative credit for time served prior to sentencing even though he had "bail set" while in custody and even though he was not charged or sentenced pursuant to a statute which required "the imposition of a minimum mandatory sentence." 2/

2/ See also <u>United States</u> v. <u>Smith</u>, 379 F.2d 628 (7th Cir. 1967).

The Stapf court reasoned that there was no legitimate basis for a classification requiring credit for pre-sentence custody for lack of bail as to a minimum term offense but unavailable in less serious offenses not punishable by a minimum mandatory sentence. The court also rationalized, without citation, that the Congress enacting the 1960 amendment made no provision for defendants sentenced for offenses not carrying mandatory minimum terms of imprisonment because it assumed that sentencing courts had been providing, and would continue to provide, credit for pre-sentence custody. (Citing Congressional hearings held long after 1960; Stapf, supra, at page 329, Footnotes 7 and 8.)

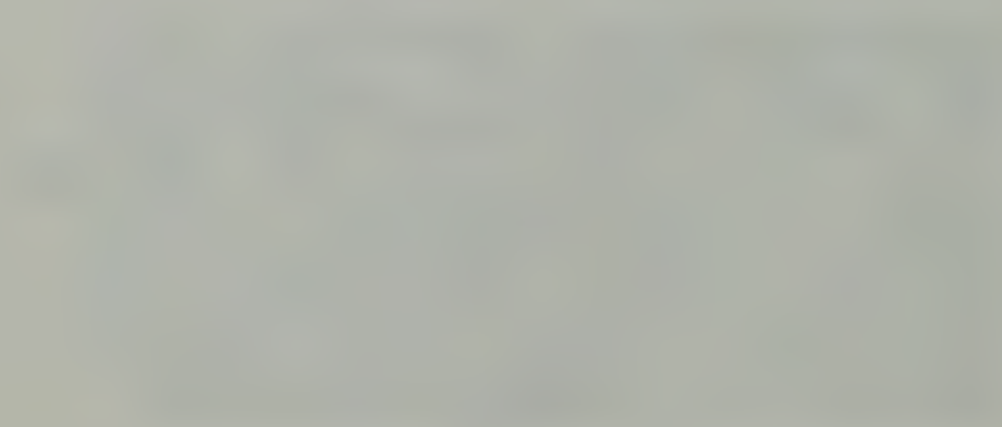
A contrary view has been expressed in other circuits. Sawyer v. United States, 376 F.2d 615 (8th Cir. 1967); Schreter v. United States, 265 F. Supp. 369 (D.C.N.J., 1967); Allen v. United States, 264 F. Supp. 420 (D.C.M.D. Pa., 1966). See also Amato v. United States, 374 F.2d 37 (3rd Cir., 1967); Scott v. United States, 326 F.2d 343 (8th Cir. 1964); Powers v. Taylor, 327 F.2d 498 (10th Cir. 1964); United States v. Abele, 269 F. Supp. 29 (E.D. La., 1967); Joseph v. United States (U.S.D.C. E.D. Louisiana), 272 F. Supp. 687 (1967).

The appellee contends that the plain, simple and unambiguous language of the 1960 amendment defies resort to judicial construction. Sawyer v. United States, supra, page 618. As pointed out in Sawyer, the legislative history of the 1960 amendment clearly shows that the purpose of Congress was the allowance of credit for time spent in custody for want of bail set where the

sentence was imposed under a statute requiring a minimum mandatory sentence. Id. at page 617, Footnote 2. Moreover, the arbitrary classification found by the Stapf court simply does not exist where one views the statutory classification as an expression of Congressional intent to require credit for pre-sentence custody time in mandatory minimum cases where the sentencing court has no discretion in the matter of sentence to set the term below the mandatory minimum. The Congressional intent may well have been to leave the matter of credit for pre-sentence custody to the discretion of the sentencing court in cases where the court could exercise complete discretion as to sentence.

B. THE SENTENCING COURT MAY NOT BE COMPELLED AT A LATER DATE TO GRANT CREDIT FOR THE TIME THAT APPELLANT SPENT IN CUSTODY PRIOR TO THE IMPOSITION OF SENTENCE WHERE IT IS POSSIBLE THAT THE COURT TOOK INTO CONSIDERATION SUCH CUSTODY TIME WHEN IT ORIGINALLY IMPOSED SENTENCE.

It is clear that the appellant in this case did not receive the maximum sentence since the two five year terms were ordered to run concurrently each with the other instead of consecutively. Title 18, United States Code, Section 500; Sawyer v. United States, 376 F.2d 615 (8th Cir. 1967); United States v. Deaton, 364 F.2d 820 (6th Cir. 1966), cert. den. 87 S. Ct. 1173, 386 U.S. 977, 18 L.Ed.2d 138; Doelle v. United States, 301 F.2d 293 (7th Cir. 1962).



It is also apparent from the record that the judge who denied petitioner's claim pursuant to Rule 35, Federal Rules of Criminal Procedure, was the same judge who sentenced the petitioner [C. T. 12, 26 and 27]. The written order denying the motion shows that the judge was aware of the fact that he was imposing less than the maximum sentence [C. T. 26]. Even assuming arguendo the validity of Stapf and Dunn, supra, these holdings are not applicable where the appellant was not sentenced to the maximum term by the sentencing court and it was therefore possible that the sentencing court considered prior custody in imposing sentence. Indeed, the Stapf court ruled that "wherever possible, as a matter of mechanical calculation, that credit could have been given, we will conclusively presume it was given." Id. at page 330. The court noted expressly that its decision was not equivalent, either in intent or effect, to a retroactive application of the 1966 amendment.

Appellant's claim for credit must be denied, where, as here, the sentence was less than the maximum; the judge who denied the request is the judge who imposed the sentence originally; and the sentence was imposed long before the effective date of the 1966 amendment to Section 3568. Amato v. United States, 374 F.2d 36 (3rd Cir. 1967); United States v. Deaton, supra; Schreter v. United States, 265 F. Supp. 369 (1967).

V

CONCLUSION

Since appellant is not entitled to automatic credit for time served in custody prior to the imposition of sentence, the order denying the Motion to Correct Sentence should be affirmed.

Respectfully submitted,

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CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ Michael D. Nasatir
MICHAEL D. NASATIR

No. 22,393

[Un]ited States Court of Appeals

FOR THE NINTH CIRCUIT

GREAT FALLS COMMUNITY TV CABLE CO., INC.,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION
and
UNITED STATES OF AMERICA,
Respondents,

HARRISCOPE BROADCASTING CORPORATION,
SNYDER & ASSOCIATES,
TELEPROMPTER TRANSMISSION OF KANSAS, INC.,
Intervenors.

On Petition for Review of an Order of the
Federal Communications Commission

BRIEF FOR INTERVENORS HARRISCOPE BROADCASTING CORPORATION and SNYDER & ASSOCIATES

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April 27, 1968

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COUNTERSTATEMENT OF THE CASE

In its Statement of the Case, Petitioner provides this Court with its own view of history and with a slanted exposition of the facts herein. Intervenors Harriscope Broadcasting Corporation (hereinafter "Harriscope") and Snyder & Associates (hereinafter "Snyder") have had an opportunity to review the Counterstatement of the Case prepared for submission to this Court by Respondent Federal Communications

Commission. With the additional comments noted hereinafter, the Counterstatement of the Case by the Federal Communications Commission is endorsed and adopted by Intervenors Harriscope and Snyder.

Petitioner's Statement of the Case contains numerous errors, distortions and exaggerations in the treatment of the history of FCC regulation of CATV and of the facts of this case:

> (1) A prime example appears in Petitioner's analysis (Brief, p. 5) of the Commission's and the Congress' consideration of CATV jurisdiction. According to Petitioner, "a 1966 bill to confer jurisdiction over CATV" was followed by the Commission's assumption of jurisdiction in 1965! Of course, as is clear from Petitioner's own reference to the legislative history (Appendix B, p. 54a), the 1966 bill looked toward *confirmation* of jurisdiction over CATV by the FCC. Certainly, the fact that the Commission looked to Congress for confirmation and clarification of jurisdiction in no way undermines the validity of its assumption of jurisdiction over CATV.
>
> (2) Petitioner far over-plays the operating history of its CATV system (Brief, p. 6). Based upon the facts provided by Petitioner itself, the CATV system has shown a steady growth and has reached a position, after six years of operation, whereby the system now expects to produce substantial profits on a relatively fixed investment. Of course, of critical importance is the fact that the growth of the CATV system is a direct concomitant of

adverse impact on the audience and rates of the local television stations.

(3) Petitioner persists in asserting that compliance with the Commission's non-duplication rule " will eliminate about 60 per cent of the service" of its Great Falls CATV system and will "destroy" the system. It has already been shown to this Court, at the oral argument on Petitioner's Motion to Stay, that the record reflects that less than 25% of Petitioner's CATV service would be affected by the Commission's Order. This percentage is based on Petitioner's own figures provided in R. 11, *et seq.* Regardless of the percentage loss of service to the Petitioner, the important fact is that the public will not be deprived of the availability on the same day of one single television program. Compliance with the Commission's Order would leave Petitioner with sufficiently attractive program offerings to insure the continued viability of its operation.

(4) In emphasizing the amount of program material required to be deleted from its systems, Petitioner neglects the elementary fact that the two local television stations in Great Falls, licensed to Intervenors Harriscope and Snyder, can, by definition, carry only two television programs at one time. Deletion of the programs carried by the Great Falls stations, on a same-day basis, would leave Petitioner with a competitively attractive array of program offerings:

(a) First and foremost, at least one entire "schedule" of national network programs will be available, since there are only two local stations and three national television networks;

(b) Assuming the correctness of Petitioner's allegation that its system can provide the signals of "the local television stations free of 'ghosting' or reception problems caused by the terrain or local interference," such benefits will continue to be provided to the public by the Petitioner;

(c) A time and weather service originated by the Petitioner over its CATV system;

(d) FM radio signals, some of which are newly added to Petitioner's system pursuant to the Commission's Order here under consideration;

(e) Programs of Educational Television Station KUED from Salt Lake City, Utah. The programming of this station will continue to be available as an incentive for the continuance of public subscription to Petitioner's CATV system.

This handsome array of program offerings constitutes the minimum which Petitioner can continue to sell to the public in and around Great Falls. Thus, present subscribers and potential subscribers to Petitioner's CATV system will continue to have substantial incentive to support the service, even as modified by requiring nonduplication protection for the local television stations.

ARGUMENT

I.

THE FCC HAS FULL STATUTORY AUTHORITY AND JURISDICTION TO REGULATE MICROWAVE-FED CATV SYSTEMS

> Petitioner maintains that the issue of jurisdiction over CATV is independent of the means of delivery of the signals, whether off-the-air or microwave-fed. (Brief, p. 10)

Petitioner's assertion, quoted above, is analytically and legally incorrect. The factual and legal distinctions between CATV systems which receive signals of television stations off-the-air, and those which are microwave-fed, have already been recognized by this Court. In *Southwestern Cable Co. v. United States,* 378 F. 2d 118, *certiorari* granted 389 U.S. 911, this Court questioned the Commission's authority to issue proscriptive orders in advance of hearing affecting a *non*-microwave-fed CATV system, but evidenced no quarrel with the heretofore undoubted Commission authority to order compliance with reasonable regulations by a *licensed* entity. This Court cited the leading case upholding the Commission's authority to regulate microwave carriers which serve CATV systems: *Carter Mountain Transmission Corp. v. Federal Communications Commission,* 321 F. 2d 359 (C.A.D.C. 1963), *certiorari* denied 375 U.S. 951.[1]

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[1] This Court also discussed *Mesa Microwave, Inc. v. Federal Communications Commission,* 262 F. 2d 723 (C.A.D.C. 1958) in terms of "a case dealing with CATV problems" and a decision dealing with "the licensing authority."

A complete analysis of the Commission's regulatory power over the microwave carrier and, consequently, its CATV customer is set forth in the Brief of Respondent Federal Communications Commission. This analysis is endorsed and adopted by Intervenors Harriscope and Snyder.

Petitioner concedes (Brief, p. 20) that the Commission has full authority to deny an application for a microwave license, upon a record finding that the proposed service is inconsistent with the public interest. A total denial of a microwave license would, of course, completely deprive a CATV system of any opportunity to provide distant signals over its system. To argue, as Petitioner does, that the Commission can deny a microwave license completely, in the public interest, but cannot condition the grant of such a license — permitting the provision of some service and restricting other aspects of the service – is legally and logically unsound.

II.

THE COMMISSION'S CAREFUL BALANCE OF CATV AND BROADCAST INTERESTS IS FAIR, REASONABLE AND RESTRAINED

From the outset, the Commission has been required to balance the competing considerations of CATV and broadcast services. After rule making proceedings, the procedural adequacy of which is not questioned by Petitioner, the Commission concluded that CATV (a) can complement the broadcast services by making available to various communities a greater choice of television and other programming, and (b) at the same time, represents a threat to local television service, particularly to service to rural areas. The threat to

off-the-air television service to rural areas is a matter of particular concern in the sparsely populated areas of western states such as Wyoming and Montana, because it is economically unfeasible for CATV systems to lay wires reaching out to sparsely populated rural areas beyond the cities and towns of concentrated population. To make the role of CATV complementary rather than antagonistic to local television service, the Commission has simply required that CATV systems not compete unfairly with the local television stations. This result is accomplished by imposing a requirement that the CATV system not duplicate, on the same day, programs provided by local stations.

The rates for advertising which can be charged by local television stations are based on the audience reached by those stations. To the extent that CATV systems furnish the same programs as are carried by local television stations, the audience of the local stations is fragmented and the revenue of such stations is decreased. When it is considered that, in the case of national television network programming, the television stations have bargained for program exclusivity in their service areas, the unfairness of the importation into the home base of the television station of signals pirated from other stations by the CATV systems, becomes apparent. Unless some restriction is placed on the development and growth and operation of CATV systems, in Great Falls and elsewhere throughout the country, the present over-the-air television system could be completely eliminated.

Petitioner's contentions that the Federal Communications Commission, absent direct licensing authority, cannot regulate CATV business; that the Commission's non-duplication rules violate the First Amendment and operate in restraint of trade; and that the Commission's Order, entered without an evidentiary hearing, was made in violation of Petitioner's

right to due process of law, have all been consistently rejected by Courts of Appeals throughout the country. See, *e.g., Buckeye Cablevision, Inc. v. Federal Communications Commission*, 387 F. 2d 220 (C.A.D.C., 1967); *Presque Isle TV Co., Inc. v. Federal Communications Commission*, ____ F. 2d ____ (C.A. 1, Dec. 18, 1967);[2] *Wheeling Antenna Company, Inc. v. Federal Communications Commission*, ____ F. 2d ____ (C.A. 4, Feb. 28, 1968); and *Conley Electronics, Inc. v. Federal Communications Commission*, ____ F. 2d ____ (C.A. 10, Apr. 22, 1968). In these decisions by the District of Columbia, First, Fourth and Tenth Circuits, the validity of the Commission's careful balance of the competing interests of CATV and local television have been recognized. The matter is concisely stated in the *Wheeling Antenna Company* decision of the Fourth Circuit:

> Nor on the merits do we see error in the Commission's judgment. Appreciation of its problems is reflected in the history of CATV's origin, its development and its relation to television nationwide. It is primarily a televisionary complement. Further, a CATV system is very largely dependent upon the existence of a live station, from which is obtained its stock in trade–TV programs. Indisputably, the service it performs is nonetheless a valuable contribution to our way of life and constitutes an important industry.
>
> Lest this companion threaten the vitality of national television, the Commission early and constantly looked for ways of blending the usefulness of both. Channel 9 Syracuse, Inc. v. FCC, 385 F. 2d 969, 970 (D.C. Cir. 1967); Second Report and Order, 2 FCC 2d 725, 745-46 (1966). Televisors were placed so as to assure both their permanence and

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[2] This matter was remanded to the FCC for further consideration of the particular facts of the case.

their service to the public, as contemplated by the Communications Act of 1934, supra, 47 USC 151, 307(b). Establishment of the contours was designed to prevent CATV from disrupting the pattern, and to keep CATV and TV in "complementary rather than conflicting roles." First Report and Order, 38 FCC 683, 699 (1955).

For its survival, of course a station needs financial support. Commercial advertisements are a chief source and these are attracted by the number of a station's viewers, for they are the advertisers' prospective customers. Consequently, to insure its permanence a station is entitled to some protection against dilution of its coverage through CATV's introduction of the same programs from more removed stations. In weighing the hurt to CATV against the help to TV, there are several considerations besides the hope of preserving the station as a local and national asset. One is the fact that the local station is put to substantial expense in procuring programs, while CATV has so far been able to use them without sharing this burden.[7]

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7 A decision holding that CATV can be subjected to copyright liability will soon be reviewed by the Supreme Court. See Fortnightly Corp. v. United Artists Television, 377 F. 2d 872 (2 Cir. 1967), cert. granted, 36 USL Week 3226 (U.S. Dec. 5, 1967) (No. 618).

> On balance, we cannot say the Commission has not been impartial in fulfilling its obligations. Neither the rules nor their administration are shown to be unjust, including the particular rule now in suit. Seemingly, it represents a fair adjustment and accommodation of conflicting claims to first place in the public interest. Cf. Channel 9 Syracuse, Inc. v. FCC, supra, 385 F.2d 969, 971, and Carter Mountain Transmission Corp. v. FCC, supra 321 F.2d 359, 363, cert. den. 375 US 951. The Commission's order is an even-handed and justified execution of this policy. . . .

The decision of the Tenth Circuit Court of Appeals in *Conley Electronics Corporation v. FCC, supra,* by Chief Judge Alfred Murrah, is not only the most recent Court of Appeals decision in this area but also a most comprehensive refutation of allegations similar to those made by Petitioner herein. As that Court stated the questions, there were challenged therein (a) the validity of the Commission's non-duplication rule, based upon the assertion that it is outside the jurisdiction of the Commission and violative of the First Amendment; and (b) the Commission's failure to provide an evidentiary hearing, as violative of various procedural statutes and constituting a deprivation of due process of law. The Court specifically noted that the Commission's adoption of the non-duplication rules was based upon its determination that, otherwise, CATV systems would engage in "unfair competitive practices" and its concern that, ultimately, CATV might deprive the public as a whole of free television service, particularly service to outlying areas, and local service with local control and selection of programs. The Court, in essence,

completely affirmed both the Commission's jurisdiction and authority to adopt the non-duplication rule, and its application thereof to the CATV system involved in that case. Reference to the facts in the *Conley* case will quickly reveal that the Petitioner in this case has made no significantly different allegation of fact which would warrant different treatment.

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April 27, 1968

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

STANLEY B. COHN

ed States Court of Appeals

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FOR THE NINTH CIRCUIT

No. 22,393

GREAT FALLS COMMUNITY TV CABLE CO., INC.,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION
and
UNITED STATES OF AMERICA,

Respondents,

HARRISCOPE BROADCASTING CORPORATION,
SNYDER & ASSOCIATES,
TELEPROMPTER TRANSMISSION OF KANSAS, INC.,

Intervenors.

On Petition for Review of An Order of the
Federal Communications Commission

BRIEF FOR PETITIONER

JURISDICTIONAL STATEMENT

This is a petition for review of a memorandum opinion and order of the Federal Communications Commission (10 F.C.C.2d 656,R. pp. 60-84), released November 17, 1967,

ordering petitioner and other parties to comply with Sections
21.712 and 74.1103 of the Commission's Rules. 47 C.F.R.
21.712, 74.1103. The petition for review was filed under
Section 402(a) of the Communications Act of 1934, as amen
ed. 66 Stat. 718 (1952), 47 U.S.C. 402(a), and Sections 2 an
3 of the Judicial Review Act, 64 Stat. 1129, 1130 (1950), 2
U.S.C. 2342 and 2343.

STATEMENT OF THE CASE

This review broadly challenges the jurisdiction of the Fe
eral Communications Commission to regulate community an-
tenna systems (CATV), whether operated from "off-the-air"
reception or through common-carrier microwave service. Spe
cifically, the review is directed to the validity of the "non-
duplication" rule as contained in Sections 21.712 and 74.11
and petitioner's forced compliance with these rules. Before
examining the facts of the case a brief background and expla
nation of CATV operation and its treatment by the Federal
Communications Commission is in order.

1. History of CATV

The FCC has defined a CATV system "as a facility whi
receives and amplifies the signals broadcast by one or more
television stations and redistributes such signals by wire or ca
ble to the homes or places of business of subscribing member
of the public for a fee." *First Report and Order,* 38 F.C.C.

683, 684, N. 1 (1965).[1] Ordinary television transmission is geographically limited to line of sight, usually about 70 miles due to the earth's curvature. CATV can overcome terrain barriers and extend the limited range by erecting a high antenna tower within the line of sight transmission and by piping the signals received through connecting cable lines. Still further extension of television signals can be made by using microwave transmission; that is receiving the signals within the broadcast range and by beaming them along a point to point radio air wave and then through the connecting cable at the viewing location.

CATV systems selling this service since 1950 are nearly as old as commercial television. The systems first brought signals to areas which had no television, either because they lay behind a mountainous shield or were too remote to available television broadcasting. Advances in technology enabling multiple signal transmission along the same cable, broadened CATV service to include bringing other network programming to areas with only one station. Current industry development permits carrying 40 signals on the same cable, much more than are available off the air, and has brought CATV service into major metropolitan areas, offering quality reception free of interference and closed circuit programming originated by the system.

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[1] This Court has dealt with CATV Issues in *Southwestern Cable Co. v. United States*, 378 F. 2d 118 (9th Cir., 1967), *cert. granted*, 389 U.S. 911 (1967); *Cable Vision, Inc. v. KUTV, Inc.*, 335 F. 2d 348 (9th Cir., 1964), *cert. denied*, 379 U.S. 989 (1965). Presently pending before the Court is *Total Telecable, Inc. v. Federal Communications Commission*, No. 21990, submitted November 10, 1967, but held in abeyance pending the outcome of *Southwestern, supra*.

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1. History of CATV

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2. CATV Regulations

Federal regulation of CATV is a recent reversal of the Commission's repeated disclaimer of any jurisdiction over CATV systems. Initially and dating from the early 1950's, Commission action affecting CATV concerned the grant of radio licenses to construct and operate common carrier microwave radio stations serving CATV systems. This licensing conformed to traditional common carrier approvals, reviewing rates and discriminatory practices. Under the Commission's common carrier licensing, microwave CATV systems sprang up all over the country enabling every area to have television reception.

In 1956, the Commission issued rules regarding the limits of cable radiation of energy by CATV systems. This action was consistent with the Commission's practice of protecting radio and television signals from interruption by electrical interference. In 1959, after a two-year investigation of "auxiliary" services of television broadcasting, the Commission issued a report and order holding that it did not have jurisdiction under the Communications Act of 1934 to regulate CATV systems, whether the systems were off-the-air or microwave fed and that economic protection of broadcasting was an "absurdity" *CATV and TV Repeater Services,* 26 F.C.C.403, 429, 431-432 (1959).[2]

After this disclaimer of jurisdiction over CATV, the Commission requested Congress to pass certain remedial legislation conferring limited jursidiction over CATV. The proposed legislation contained in S. 2653, 86th Cong., 1st Sess. (1959) was

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[2] Parts of this ruling relating to Commission jurisdiction over CATV are set forth in Appendix A, pp. 1a-9a.

defeated after long and bitter debate by a vote to recommit the bill. A second attempt by the Commission in 1961 to gain jurisdiction over CATV died in committee. A 1966 bill to confer jurisdiction over CATV also failed.[3]

Following these unsuccessful attempts to obtain Congressional grant of jurisdiction, the Commission assumed jurisdiction and issued its *First Report and Order,* 38 F.C.C. 683 (1965), requiring *microwave*-CATV systems, upon request, to carry the signals of all local and nearby television stations and to refrain from duplicating the programs broadcast by the local stations. The adoption of these rules was based on the conclusions that CATV competition is unfair and action is needed to ameliorate the adverse affects of this competition for the maintenance and healthy growth of television broadcast service (38 F.C.C. at 713). In short, the regulations were designed to provide economic protection to licensee broadcasters, by restraining the business conduct of non-licensee CATV systems.

A year later the Commission issued its *Second Report and Order*, 2 F.C.C.2d 725 (1966), applicable to *all* CATV systems and providing for local carriage and non-duplication. Two Commissioners dissented from the promulgation of these rules adhering to the prior decision that the Commission had no statutory authority or jurisdiction over CATV, 2 F.C.C.2d at 808 and 819.[4]

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[3] A legislative history of the Commission's unsuccessful attempts to gain jurisdiction is contained in Appendix B, p. 37a.

[4] These dissents are quoted in full in Appendix A, pp. 24a and 26a. See also Loevinger dissents in same proceedings, Appendix A at pp. 10a and 27a.

3. CATV in Great Falls, Montana

The Great Falls Community TV Cable Company, Inc., was established in 1961. It carries eight television signals— two local signals and eight imported. In addition, it originates and carries a time and weather station. Of the imported signals, three are from Spokane, Washington (KREM, KXLY, and KHQ), one from Lethbridge, Canada (CJLH), and two from Salt Lake City, Utah (KUED and KCPX). The three stations from Spokane, and the one from Canada are received by common carrier microwave of TelePrompTer Transmission of Kansas, Inc., and the two from Salt Lake City by microwave of Western Microwave, Inc. Local stations are received off-the-air by ordinary CATV antenna. (R. p. 4).

The Great Falls system has grown slowly and unprofitably. It began in December of 1961 and by the end of 1962 had 800 subscribers. At the end of 1963, it had only 1100 subscribers; and by 1964, 2400; by 1965, 3100; by 1966, 4100; and at present, 5069 subscribers. (R. p. 19) During its six year period of operation, the CATV system has spent approximately $10,000 a year in advertising and promotion. More than $820,000 is invested in plant with a present value of $525,000. (Symons affidavit attached to Motion for Stay, para. 6). To date, the system has not produced a net profit in any year of operation. However, net losses are down from a high of $97,000 in 1964 to a low of $12,000 for the past year. With its current subscription and a projection of future subscribers in its potential market, the system expects to produce a net profit in the immediate years of operation and realize a steady return on the substantial investment. (R. p. 20).

Great Falls has two local television stations, KFBB-TV, founded in 1954, and KRTV, founded in 1958. Both are

affiliated with national networks, KFBB-TV with CBS and ABC, and KRTV with NBC and ABC. Thus, citizens of Great Falls have available by off-the-air reception a substantial majority of network television programming. The principal service or marketable feature offered by the CATV system in Great Falls is a broader selection of competing network television shows only available off-the-air at the same time. Since approximately 80 percent of the imported television signals carried by the CATV come from an earlier western time zone, the local viewer can enjoy competing programs offered only simultaneously by local television, but available at other times by the CATV carriage. (R. p. 40-41).

Enforcement of the non-duplication order will eliminate about 60 percent of the service of the system and destroy its unique, marketable feature. Non-duplication will result in almost certain destruction of CATV in Great Falls and deprive subscribers of their preferred free selection. (R. pp. 40,42).

4. The Proceedings before the FCC

Petitioner, Great Falls Community TV Cable Co., Inc., is not a licensee or applicant for license before the FCC. The FCC does not purport to "license" the conduct of a CATV business. However, petitioner's affiliate and intervenor here, TelePrompTer Transmission of Kansas. Inc., is a licensee of several common carrier microwave stations used in importing the Canadian and the three Spokane signals to Great Falls. Permission to build and operate these systems was licensed in 1961 and was not then subject to any restrictive conditions affecting carriage by the CATV customer.

On September 15, 1965, TelePrompTer Transmission of Kansas, Inc., filed an application with the FCC for

modification of its licenses of stations servicing Great Falls CATV to add FM radio signals and for waiver of the newly promulgated non-duplication rules. These rules provide that no additional service would be approved for existing microwave licensees without promise of non-duplication of local television. The proposed service by TelePrompTer was not for television carriage but was an extension of FM radio programming to Great Falls, Montana.

On March 8, 1966, the Commission further extended its jurisdiction over all CATV systems (whether using microwave or not) and similarly required non-duplication by CATV systems. *Second Report and Order*, 2 F.C.C. 2d 725 (1966). On April 18, 1966, TelePrompTer Transmission of Kansas, Inc., was joined by its affiliate in the proceeding, Great Falls Community TV Cable Co., Inc., which requested partial waiver of the non-duplication rule, 74.1103.[5] The local stations opposed the waiver applications.

By Memorandum and Order of November 17, 1967, and combined with various other petitions pending in the same Montana area and involving similar issues, the Commission denied the application for modification of licenses and the waiver of the non-duplication rules. In addition, the Commission issued a proscriptive order requiring petitioner to provide non-duplication protection under the Rules to the local stations within thirty days from the issuance of the order. It is this order that is here on review. By order of January 10, 1968, this Court stayed the Commission Order insofar as it affects

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[5] Petitioner had advised both the FCC and the two Great Falls TV stations that it would agree voluntarily to protect all of the programs broadcast by the two local stations for *simultaneous* duplication by programs received on the cable from the more-distant stations (R. p. 4).

petitioner's operation pending final hearing and determination of the petition for review.

SPECIFICATION OF ERRORS

1. The Commission erred in stretching its jurisdiction over non-licensee CATV systems through its recognized regulatory jurisdiction over common carrier microwave radio.

2. The Commission erred in confusing its protection of the public interest to free access and equality of rates in the use of common carrier service with its public interest considerations in the allocations of radio frequencies.

3. The Commission erred in usurping jurisdiction over CATV systems, contrary to its controlling statute and in conflict with its prior administrative rulings.

4. The Commission erred in promulgating non-duplication rules restricting the reception and distribution of information as a prior restraint in the exercise of free speech in violation of the First Amendment.

5. The Commission erred in the issuance of a summary order without hearing against a non-licensee threatening total destruction of its six-year business as a taking of property in violation of the due process clause of the Fifth Amendment.

6. The Commission erred in promulgating regulations which are unreasonable and arbitrary in discriminating against legitimate CATV competition and in delegating enforcement power of the regulations to the favored competitor broadcaster.

I.

The FCC Cannot Extend Its Jurisdiction Over Non-Licensee CATV Systems through Its Recognized Regulatory Jurisdiction Over Common Carrier Microwave Radio

The Commission maintains that it has statutory authority to impose restrictive regulations upon CATV systems through its ordinary licensing power over the common carrier microwave radio licensee, irrespective of its doubtful direct jurisdiction over CATV systems.[6] Petitioner maintains that the issue of jurisdiction over CATV is independent of the means of delivery of the signals, whether off-the-air or microwave fed. The Commission cannot impose regulation upon the CATV system through the guise of licensing of the microwave carrier, while requiring all affirmative obligations and performance by the CATV system itself. In Part I we discuss the identity of legal position between CATV systems, receiving signals either by microwave or off-the-air reception, whereas in Part II, we examine the statutory limits of the jurisdiction of the FCC to regulate any CATV. Also discussed in Part I, Section B, is the right of the user of common carrier service to receive materials without limitation or restriction, and that the protected

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[6] The Commission's general jurisdiction to regulate directly *non-microwave CATV systems* is now under review by this Court in *Total Telecable, Inc. v. Federal Communications Commission*, No. 21990, submitted on November 10, 1967, but held in abeyance pending the outcome of the review of this Court's decision in *Southwestern Cable Co. v. United States*, 378 F. 2d 118, (9th Cir., 1967), *cert. granted* 389 U.S. 911 (1967). *Southwestern*, while also raising the issue of Commission jurisdiction over non-microwave CATV, involves principally CATV rule 74.1109 and the right of the Commission to issue proscriptive orders, giving temporary relief prior to supporting findings in an adjudicatory hearing.

public interest in common carrier regulation is free access and non-discrimination in the use of common carrier service.

A. The Commission Lacks Jurisdiction over CATV Systems Irrespective of Whether the Signals Are Received Off-the-Air or by Microwave.

The *First Report and Order (CATV),* 38 FCC 683 (1965) asserts microwave CATV regulatory authority and issues rules for its conduct. Basic to these rules is Section 21.712, providing for CATV non-duplication protection of local stations by microwave-fed CATV systems. The *Second Report and Order (CATV),* 2 FCC 2d 725 (1966), issued a year later, promulgated rules applicable to *all* CATV systems, whether using microwave service or not, 47 C.F.R. 74.1101 *et seq.* This second set of rules also contains a non-duplication rule, 74.1103, which embraces, but enlarges the requirements of 21.712.

Section 21.712, while initially addressed to the microwave carrier, operates only against the CATV system. Subparagraph (a) of Section 21.712 instructs the microwave carrier to require certification of compliance from its CATV customer. The remaining parts of 21.712, (b) through (i), apply directly to the CATV system. These subparagraphs contain the carriage and non-duplication rules, identical to those directed against the CATV system in Section 74.1103. Thus, under 21.712, the Commission makes the microwave carrier merely a conduit of regulatory power and requires compliance, not by the carrier, but by the customer user.

Indeed, the Commission's rules in 21.712(j) provide that any dispute or complaint by the broadcaster concerning compliance with the non-duplication rule by the CATV system does not impose a duty upon the microwave carrier, but is to

be settled by the Commission itself. In the instant case subsequent to filing the petition for review in this Court and subsequent to this Court's order staying the effects of the Commission Memorandum and Opinion, intervenor broadcasters applied to the Commission for an order compelling enforcement of non-duplication by the microwave carriers. By order released February 14, 1968, the Commission quite properly dismissed the motion in compliance with this Court's order and explained the role of the microwave carrier:

> This provision [Section 21.712(j)] was added to the rules to clarify the Commission's policy that the common carrier's role in the case of disputes is a *passive* one; that it does not have the burden of interpreting, applying and enforcing the carriage and non-duplication provisions of the Rules; and that it is not liable under Section 206 of the Communications Act where a CATV-TV dispute arises. [Emphasis added] (*Western Microwave Inc.*, FCC 68-110, 1153 released February 14, 1968, pp. 4, 5.)

Admittedly then, the microwave carrier stands only as a dumb, passive, jurisdictional fiction to reach the non-licensee CATV operator, in whom rest all the burdens, duties, and liabilities for compliance.

In practical operation, it is the CATV system which must take the affirmative action to comply with these rules, since mechanically the non-duplication is achieved at the "head-end" of the CATV system; that is, the microwave carrier pipes in the same program material, but the CATV system through the use of auxiliary equipment itself blacks out or eliminates the proscribed "duplicating" program before sending the signals through its cable connections.

Thus, Rule 21.712, which ostensibly is addressed to the license carrier, imposes no restrictions upon the material transmitted over the carrier circuit. Indeed, the FCC has no interest in the volume or nature of program transmission by the jurisdictional carrier. Rather, the express intent of Rule 21.712 is to prescribe the use which the carrier's customer may make of the programs delivered to it over the carrier circuit, and for which the customer pays full transmission charges.

Petitioner does not dispute the jurisdiction of the FCC to license and regulate common carrier microwave stations. Indeed, regulation as to tariffs and radio transmission are essential elements of the FCC's function in protection of the public interest as well as the customer served. Petitioner *does* challenge the right and jurisdiction of the FCC to reach the CATV system, over which it has no jurisdiction, by the device or ruse of regulating the microwave carrier, over which it has only ordinary common carrier licensing power and regulatory control. The Commission cannot do by indirection what it cannot do by direction.

The broad implication of such an extension of jurisdiction is to reach and regulate all customers using common carrier service. In his dissent to the *First Report and Order,* Commissioner Loevinger observed:

> The most important and fundamental legal objection to the present Commission action is its lack of adequate jurisdictional basis. The rule promulgated by the Commission at this time undertakes to regulate the programs that may be carried by CATV's by requiring common carriers that serve the CATV's to impose upon their customers, as a condition of service, the limitations contained

> in the Commission rules. The Commission has repeatedly rejected this basis of jurisdiction in the past, as appears from the cases cited and quoted below. But regardless of lack of support in precedent or statutory language, the logical implications of this approach should warn of its unsoundness. If the Commission can impose its will on a person or business entity, that is the customer of a common carrier, by the simple device of requiring the common carrier to act as the Commission's policeman in order to keep its license, then the Commission can regulate any business in the United States. Every business and most citizens are customers of the telephone and telegraph companies. It has never previously been suggested that this fact subjected them to regulation by the FCC. But if today's decision stands, then that is the law. The Commission need no longer be constrained by any technical limitations on its jurisdiction arising from statutes enacted by Congress, if this theory is sustained by the courts. The rule adopted by the Commission today applies to CATV's served by the telephone company as well as to those served by CATV relay companies. But there is nothing in the logic of the Commission's jurisdictional approach that limits this technique to CATV's. If this jurisdictional foundation is sound for CATV's, the Commission may, by precisely the same technique, impose its regulations on theaters or newspapers, on stockbrokers or taxicabs, indeed on any business or person that needs and uses the services of a communications common carrier. (38 FCC 752)

As Commissioner Loevinger reasons, the logical implication of the Commission's action in reaching the customer through its

legitimate jurisdiction over the microwave carrier is to extend regulatory jurisdiction and control over almost every facet of American business by controlling the flow of information and material.

The Commission itself has previously refrained from such a device in extending its jurisdiction over the major networks. Like CATV, the major networks use microwave service to transmit packaged programs. As the principal supplier of program materials, networks naturally affect the Commission's national allocation scheme– the principal argument advanced for asserting jurisdiction over CATV. A denial or grant of a network contract for affiliation may mean life or death of a local station. This has been particularly true in UHF station operation.[7] Despite this heavy impact of network activity on broadcasting, which is the asserted basis for jurisdiction over CATV, the Commission has repeatedly and explicitly disallowed authority over the networks. In *Don Lee Broadcasting System*, 14 F.C.C.993 (1949), the Commission stated:

> The network regulations are designed to insure that control of the individual stations is not forfeited to a network organization with which such stations are affiliated. The networks, as such, are not licensed by the Commission and are under no statutory obligation to serve the public interest. The Chain Broadcasting Regulations, therefore, are designed to govern

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7 "The inability of most UHF stations to obtain network affiliation, or if affiliated, to obtain sufficient network commercial programs was an important factor in the limited development of the UHF service." Network Broadcasting, Report of the Committee on Interstate and Foreign Commerce, H.R. Rep. No. 1297, 85th Cong., 2d Sess., 226 (1958).

> the conduct of the individual stations rather than the networks . . . .

Moreover, the Commission has expressly advised Congress that it "has no jurisdiction over networks as such and the Commission does not have authority to license or regulate networks."[8] And that it "cannot reach networks directly." [9] Direct regulatory control over networks has only been sought (and unsuccessfully) through application for such authority from Congress.[10] The assertion of jurisdiction over CATV through the microwave carrier is a flat and absolute contradiction with the disclaimer of jurisdiction over networks.

In *Federal Power Commission v. Pan Handle Eastern Pipe Line Co.*, 337 U.S. 498 (1949), the FPC under its controlling statute was empowered to issue certificates of convenience and

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[8] H.R. Rep. No. 1297, 85th Cong., 2d Sess., 628 (1958).

[9] Hearings before a Subcommittee of the House Committee on Interstate and Foreign Commerce, *Responsibilities of Broadcasting Licensees and Station Personnel*, 86th Cong., 2d Sess., 672 (1960).

[10] With the support of the Commission, two bills were introduced in the 86th Congress. One was H. R. 5042 (entitled in part "A Bill To Amend the Communications Act of 1934 To Subject Television Networks to Certain Controls "), and the other was H. R. 11340 (entitled in part "A Bill To Amend the Communications Act of 1934 . . . To Provide for the Regulation of National Networks"). H. R. 5042 provided authority for the Commission to make rules and regulations directly applicable to the television networks, while H. R. 11340 provided for the exercise of regulatory authority over the networks under a mandatory system of licensing national networks. Each was designed to give the Commission specific regulatory authority over the networks. See H. R. Rep. No. 281, 88th Cong., 1st Sess., 149-50 (1963). Neither bill was enacted, and similar legislation, introduced in the 87th Cong., 1st Sess. as S. 2400, also failed of enactment.

necessity for interstate transportation and sale of natural gas and "to do the things appropriate to carry out the provisions of the Act." The Supreme Court held that this general power over gas producers and broad power to carry out the intentions of the Act did not empower the Commission to approve the sale of leases of gas reserves, even when the leases involved were used to justify the issuance of the certificates of convenience and necessity. Thus, the Supreme Court, while recognizing a general jurisdiction over gas producers, did not condone a broad control over every phase of its business activity. In the instant case, the Commission has transgressed much further than the Federal Power Commission. It seeks not to limit and control any activity by microwave common carrier, for it may carry the same material undiluted, but seeks to limit and control the business activity of the common carrier's customer – the CATV system. All of the affirmative action for compliance with the rules must be performed by the unlicensed CATV system.

Similarly, *Alaska Airlines v. Civil Aeronautics Board*, 257 F. 2d 229 (D.C. Cir., 1958), *cert. denied* 358 U.S. 881 (1958), limited the Board's control over depreciation practices of airlines, notwithstanding its general and broad authority to control the economic practices of the airlines under its jurisdiction. Jurisdiction did not confer control over *all* of the business activity of its licensees. Here, it is not only the extent of authority which is at issue, but whether jurisdiction can be stretched to cover an entirely different class of persons, not heretofore regulated or licensed by the Federal Communications Commission.

In *Regents of the University System of Georgia v. Carroll*, 338 U.S. 586 (1950), the Commission had refused a renewal of a license unless the station owner repudiated a contract for operation and management of the station. In permitting a

damage action between the contracting parties, the Court defined the ambit of the Commission's jurisdictional reach. The Commission's authority was, of course, limited by its controlling and creating statute which empowered it to exercise regulatory control only with the respect to the issuance of licenses.

> Congress has enabled the Commission to regulate the use of broadcasting channels through a licensing power. It is in connection with this power that Section 303(r) is to be interpreted. The Commission may impose on the applicant conditions which it must meet before it would be granted a license, but the imposition of the conditions cannot directly affect the applicant's responsibility to a third party dealing with the applicant. 338 U.S. at 600.

The Court observed that the Commission had applied for additional authority to issue cease and desist orders, which subsequent to the decision was granted, but "the Commission request did not go beyond asking for power to issue a cease and desist order against a licensee. *No power was sought against a third party.*" [Emphasis added] 338 U.S. at 602. Here the Commission's authority is similarly restrained against imposing any regulations or restrictions or by enforcing any such regulations and restrictions against a third party. It is not merely an issuance of the licenses through which the Commission now seeks to assert its control over microwave users (although it conditions grants of licenses on user contracts promising non-duplication). However, it is the continuing exercise and performance imposed, not upon the licensee microwave carrier, but upon the third party non-licensee user. The licensee microwave carrier's activity and revenue remain unchanged, except that he becomes the conduit of jurisdiction. It is the ultimate user who has become subject to an entire

new scheme of regulatory power and without any protections or rights afforded to ordinary licensees by the Commission.

The Commission's jurisdiction over microwave must stand upon whether or not it can regulate CATV systems directly. It is the ultimate purpose and action which must be judged in determining the Commission's jurisdiction. The Commission itself maintains that it has this broad jurisdiction, and if so, it does not have to proceed behind a screen by manipulating the license of the microwave carrier. On the other hand, if the Commission lacks the jurisdictional authority over CATV systems, it cannot gain it through the back door by regulations addressed to the microwave carrier but operable only against CATV systems. Radio licensing jurisdiction over microwave carriers is not regulatory control over these microwave carriers for any and all purposes; it is limited to reasonable regulation to perform microwave common carrier service. It does not extend to the control over the business activity of the common carrier's customer.

The *First Report and Order, supra,* contains no jurisdictional statement. The Commission relies principally upon its statement in *Carter Mountain Transmission Corp.,* 32 F.C.C. 459 (1962), which was affirmed in *Carter Mountain Transmission Corp. v. Federal Communications Commission,* 321 F. 2d 359 (D.C. Cir., 1963), *cert. denied,* 375 U.S. 951 (1963). This jurisdictional position is examined at length in Commissioner Loevinger's dissent, 38 F.C.C. at 756,[11] which explains that *Carter Mountain* involved a CATV relay company in its application for authority to transmit television signals by microwave to a small community with one local television station. After an evidentiary hearing, the Commission found that the grant of

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[11] Quoted in full, Appendix A, p. 19a.

the microwave authority would destroy the local television station. Thus, the case turned upon the public interest factors in the grant of a specific license. The Commission's opinion stated:

> There is no attempt to examine, limit, or interfere with the actual material to be transmitted. We are merely considering the question of whether the use of the facility is in the public interest, a conclusion which must be reached prior to the issuance of the grant. (32 F.C.C. at 463).

This decision provides a thin precedent for the jurisdiction that the Commission now asserts over CATV systems. Without examination, the D.C. Circuit broadly approved the Commission action and invited further extension of jurisdiction. Relying on *Carter Mountain* the same court approved without further examination CATV jurisdiction through the microwave carrier in *Idaho Microwave, Inc. v. Federal Communications Commission*, 352 F. 2d 729 (1965). However, the D.C. Circuit, which broadly favors the extension of administrative jurisdiction and control, without examining the legislative history and on the very narrow issues presented to it, has broadly upheld Commission jurisdiction over all CATV in *Buckeye Cablevision Inc. v. Federal Communications Commission*, ____ F. 2d ____ (D.C. Cir., 1967), in conflict with this Court's earlier holding in *Southwestern Cable Co. v. United States*, 378 F. 2d 118 (9th Cir., 1967), *cert. granted*, 389 U.S. 911 (1967). No other circuit has given judicial approval to these rules[22] and it is submitted that the D.C. Circuit's holding is not persuasive.

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[22] Action challenging the validity of these rules was pending in a number of circuits, including the D.C. Circuit, which were transferred and consolidated in the Eighth Circuit in *Black Hills Video Corporation et al. v. United States*, Nos. 18,952 and 18,548.

Ultimately, the Commission's jurisdiction must stand or fall on its direct jurisdiction over CATV systems themselves. This jurisdiction must be judged in the context of what the Commission seeks to accomplish and what parties or activities the Commission intends to control.

B. The Commission Cannot Restrict or Regulate the Content of Material Carried by Common Carrier Microwave Service Since This Regulation Impinges the Customer's Right of Access to and Equality of Service.

Under the Communications Act of 1934, a common carrier is "any person engaged as a common carrier for hire in interstate or foreign communication by wire or radio . . ." 47 U.S.C. 153 (h). Microwave transmission of television signals is a common carrier service. *Mesa Microwave, Inc. v. Federal Communications Commission*, 262 F. 2d 723 (D.C. Cir., 1958), and as such is subject to common carrier regulation under Title II of the Communications Act. 47 U.S.C. 201-222. The Commission originally held that regulation of common carrier facilities did not properly include the lawful use of those facilities by CATV systems. *CATV and TV Repeater Services*, 26 F.C.C. 403, 432-433 (1959):

> 75. We are of the opinion that, in relation to the authorization of a common carrier facility, whether it be for a radio facility under title III of the act or a wire facility under title II, it is neither proper, pertinent, nor necessary for us to consider the specific lawful use which the common carrier subscriber may make of the facilities of the carrier. To take a different view would place the

> Commission in the anomalous position of acting as a censor over public communications, and put us under the burden of policing, not only the use of such facilities but the content of communications transmitted on the facilities. The logical extension of such a philosophy would require us to deny communications facilities of any kind (message telephone, telegraph, etc.) to CATV's and, for example, to deny access to facilities to those acting contrary to our concept of the public welfare. The adjudication of these matters is beyond our province.

This view is consistent with the provisions in Title II of the Act. Section 201 obligates the common carrier to furnish free access and availability upon reasonable request for service. Discrimination and preferences in charges, facilities or services are prohibited by Section 202(a), 47 U.S.C. 202(a). The Act directs the Commission to examine transactions entered into by common carriers which affect the services rendered and to report to the Congress whether any transactions are likely to affect adversely the ability of the carrier to render adequate service to the public. 47 U.S.C. 215(a). Common carrier service cannot be arbitrarily or discriminatorily applied or withheld, but the public has a right to demand common carrier communication service. *Pulitzer Publishing Co. v. Federal Communications Commission,* 94 F. 2d 249, 251 (D.C. Cir., 1937).

At the root of common carrier service, whether it be transportation or communication, is availability to all users on the same terms and conditions. *Seaboard Airline Railway Co. v. United States,* 254 U.S. 57 (1920); *New York v. United States,* 331 U.S. 284, 296 (1947). Here, the common carrier rules are subverted for jurisdictional purposes and used in conflict with the essential character of common carrier service—

free access and non-discrimination. The Commission in protecting the public's right to free access and equality of service is limited by the terms of the Act from imposing discriminatory treatment or conditions.

Common carrier service and radio broadcasting present two distinct problems covered in different parts of the Communications Act. This distinction is recognized in *Federal Communications Commission v. Sanders Brothers Radio Station*, 309 U.S. 470, 474 (1940):

> In contradistinction to communication by telephone and telegraph, which the Communications Act recognizes as a common carrier activity and regulates accordingly in analogy to the regulation of rail and other carriers by the Interstate Commerce Commission, the Act recognizes that broadcasters are not common carriers and are not to be dealt with as such . . . .

See also *Allen B. Dumont Laboratories, Inc. v. Carroll*, 184 F. 2d 153 (3rd Cir., 1950); *United States v. Radio Corporation of America Communications*, 358 U.S. 334, 348-350 (1959). The Commission recognized the distinction between the two regulatory schemes in *Southeastern Enterprises (WCLE)*, 22 F.C.C. 605, 615 (1957): "Congress has not given us the power, as in the case of the carriers that we regulate under Title II, to regulate the business of a broadcast licensee."

Both parts of the Act have the same statutory criterion – the public interest, convenience and necessity – which must be satisfied in licensing both broadcast stations and common carriers. However, this statutory standard is subject to vastly different interpretations when applied to the different services. Public interest criterion in the field of common carrier

licensing "is not a mere general reference to public welfare" but relates particularly to the "adequacy of [common carrier] service, to its essential conditions of economy and efficiency, and to appropriate provision and the best use of [its] facilities." *Texas v. United States,* 292 U.S. 522 (1934). The Commission explained the differences in *CATV and TV Repeater Services,* 26 F.C.C. 403, 432 (1959):

> In the case of the common carrier applicant, in addition to the showing of legal, technical, financial, and other qualifications, there is, typically, the necessity for showing that there are no other public communication facilities available to do the specific job proposed; that the applicant is ready, able, and willing to serve all members of the public who may desire the service, without discrimination; and that there is now in being one or more members of the public who require the service, or some reasonable expectancy that one or more such persons will present themselves if the facility is authorized. *There is no examination of the "content" of the intelligence which is to flow over the communication circuit.* [Emphasis added.]

See also *Pulitzer Publishing Co. v. Federal Communications Commission,* 94 F. 2d 249, 251 (D.C. Cir., 1937). Thus, the public interest in a national scheme of television allocations is quite different from the public's right of free access to common carrier service, and the statutory powers and obligation to enforce the latter may not be subverted in promoting the immediate policy of the former.

In the instant case the Commission seeks to limit and control the use of common carrier service by imposing a set

of regulations on the activity of the user of common carrier service. The "privilege" of any common carrier microwave service for the transportation of television signals is made conditional upon guarantees of non-duplication and exclusivity to be carried out and enforced by the customer CATV system. Thus, the Commission's rules strike at the very heart of the user's right to common carrier service. There is no precedent for such unbridled use of federal regulatory power where the access to common carrier service or public utility service in the conduct of legitimate business activity is conditioned upon compliance and adherence to discriminatory standards and rules which the Commission seeks to impose in order to protect a favored class of licensees. Even if the Commission were empowered to protect a favored class of broadcasters by restraining trade and competition, it may not do so at the expense or diminution of the public's right to common carrier service. Protecting this public right is a disparate function of the Commission's duties distinguished from its licensing of radio in the public interest. In confusing the two functions the FCC does disservice to both.

In *American Trucking Association, Inc. v. Federal Communications Commission,* 377 F. 2d 121, 130 (D.C. Cir., 1966), *cert. denied,* 386 U.S. 943 (1967), the court explained that Section 202(a), 47 U.S.C. 202(a), was a flat bar against *any* discrimination by *any* means or *any* undue preferences to *any* person. That case upheld the Commission's ruling against rate preferences imposed in common carrier telephone service using microwave transmission. Here, it is the Commission's rules governing microwave transmission which unduly discriminate against the CATV user of the common carrier service in favor of the broadcast user. In effect, the Commission maintains that it can compel the common carrier to do by regulation what would be unlawful for the carrier to do under the Act.

If the common carrier is prohibited by the Act from discrimination and preferences in service, *a fortiori* the Commission charged with the enforcement of the Act is restrained from requiring discriminatory and preferential treatment in the use and distribution of common carrier service.

The courts have consistently and repeatedly struck down discriminatory practices by common carriers which give a competitive advantage to one user over another, *New York, New Haven, and Hartford Railroad v. Interstate Commerce Commission,* 200 U.S. 361, 391-392 (1906); *United States v. Chicago Heights Trucking Co.,* 310 U.S. 344, 351 (1940). Indeed, it is the fact that the practice gives a competitive advantage in the use of common carrier service which marks it as an unlawful discrimination in violation of the public's right to common carrier service. *Union Pacific Railroad Co. v. United States,* 313 U.S. 450, 461-462 (1941). These principles of free access and non-competitive advantage apply with equal force in common carrier wire and radio communications where the common carrier sections of the Act were modeled after the ICC Act.[13]

The Commission's microwave CATV rules represent to date the broadest jurisdictional encroachment of any administrative agency. They impose a set of restrictive operational rules in exchange for the grant of a license to provide common carrier service to which the public at large is entitled; they are addressed to the licensee, but they operate exclusively against the non-licensee in the regulation of its business activity; they impose a pervasive set of rules to reduce competition of the non-licensee and in protection of a favored class of

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[13] S. Rep. No. 781, 73rd Cong., 2d Sess. 1 (1934); H.R. Rep. No. 1850, 73rd Cong., 2d Sess. 3 (1934).

licensees, the broadcasters; and they strip from the non-licensee the ordinary procedural safeguards available to all licensees.

In sum, these rules subvert the entire scheme of common carrier regulation to accomplish entirely different purposes of the agency outside of its obligation to protect the public interest in the maintenance of open and adequate common carriage for hire. In promotion of television broadcasting – a "favored class" of licensee – the rules compel a scheme of restricted access and enforced discrimination. Restrictive regulation of CATV competition through the jurisdictional medium of common carrier microwave is directly in conflict with the statutory obligation of the Commission to enforce free access and equality of service in public common carrier licensing, and, accordingly, is invalid.

II.

The Federal Communications Commission Lacks Statutory Authority To Regulate CATV Business.

A. The Substantive Titles of the Communications Act, Title II (Common Carriers) and Title III (Radio Licensing), Fail to Provide a Statutory Basis for CATV Regulation.

The Communications Act of 1934, placed under one agency unified control over all forms of electrical communications. The Act transferred to the newly created Federal Communications Commission the functions of the Interstate Commerce Commission regarding common carriers, and the functions of the Federal Radio Commission regarding radio. The provisions of the Interstate Commerce Act, 41 Stat. 475,

pertaining to common carrier regulations became Title II of the Communications Act, 47 U.S.C. 201-222, and the provisions of the Radio Act of 1927, 47 Stat. 1162, 47 U.S.C. 81 *et seq.*, became Title III of the Act, 47 U.S.C. 301-397.[14] The Act did not create any new areas of federally regulated activity. Title I created the Commission and sets forth its purposes and definitions which cover its disparate functions contained in Titles II and III.

If there is any authority or jurisdiction over CATV, it must come from either Title II or III since the other titles provide no independent substantive authority.[15] Of these two, Title II has no application, since the Commission has stated that CATV operations do not constitute common carrier activities under the Act. *Philadelphia Television Broadcasting Co. v. Federal Communications Commission,* 359 F. 2d 282 (D.C. Cir. 1966).

In attempting to establish its tenuous jurisdiction the Commission first relies upon the general purposes and definitions contained in Title I, entitled "General Provisions."[16]

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[14] S. Rep. No. 781, 73d Cong., 2d Sess. 1 (1934); H. R. Rep. No. 1850, 73d Cong., 2d Sess. 3 (1934).

[15] Of the remaining three parts to the Act, Title IV pertains to procedural and administrative requirements; Title V, penalties for violations of the Act; and VI, miscellaneous housekeeping provisions.

[16] The Commission's jurisdictional statement is contained in Appendix C to the *Second Report and Order*, 2 F.C.C. 2d at 793-797, entitled "Commission's Memorandum on Its Jurisdiction and Authority." This memorandum apparently embraces both microwave and non-microwave. We have argued in Part I that regulation over CATV may not be acquired through the conduit of the microwave common carrier, nor in derogation of the Commission's obligation

(continued)

Section 1, 47 U.S.C. 151, explains that the purposes of the Act are "regulation of interstate and foreign commerce in communication by wire and radio," and Section 2(a), 47 U.S.C. 152(a), explains that "*The provisions of this Act* shall apply to all interstate and foreign communications by wire or radio and . . . transmission of energy by radio. . . ." [Emphasis added.] Section 3(a) of the Communications Act, 47 U.S. C. 153(a), defines "wire communication" or "communication by wire" as the "transmission of writing, signs, signals, pictures, and sounds of all kinds by aid of wire, cable or other like connection between the points of origin and reception of such transmission, including all instrumentalities, facilities, apparatus, and services . . . incidental to such transmission."

Solely from these introductory provisions of the Act, the Commission argues that CATV, although not a common carrier, is "wire communication," and using the definition in 3(a) as a spring board, claims that it possesses Title III powers of regulation and rule making over CATV, as contained in Sections 4(i), 303(f), 303(h), and 307(b) of the Act. This rationale is false since: (1) Title I conveys no substantive rights but only defines terms used throughout the Act; (2) the definition of "wire communications" pertains only to Title II common carriers; (3) the legislative history indicates disparate functions over common carrier wire communication on the one hand and radio on the other, combined for convenience under one Act and with one set of definitions; and (4) Title III pertains essentially to *licensing* of radio transmission and not restriction of reception.

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16 (continued)

to protect free access to common carrier service. We argue here that the Commission likewise lacks jurisdiction to regulate CATV directly.

The Radio Act of 1927 contained a definition of "radio communication" in Section 31 (47 U.S.C. 111) which is essentially the same as Section 3(b) of the Communications Act. However, the Radio Act of 1927 contained no definition of "communication by wire" similar to Section 3(a) upon which the Commission now relies. Section 3(a) is derived from Section 1(3) of the Interstate Commerce Act (41 Stat. 475) which related only to activities of common carriers. Section 3(a) was incorporated into the Communications Act for the purpose of defining the applicability and impact of Title II powers which the FCC took over from the ICC.

Title III conferred upon the FCC the authority which the Federal Radio Commission had with respect to communication by radio and Title II conferred upon the FCC functions which the ICC had with respect to activities of common carriers. No crossover was intended and none was achieved. This intent is manifested in the Act's legislative history.[17] Moreover, the FCC has never before claimed or attempted to confuse these distinct functions. Prior to 1934, the Federal Radio Commission could not under the predecessor of Title III of the Communications Act adopt rules and regulations with respect to wire communication and, prior to 1934, the ICC could not exercise Title III powers with respect to persons engaged in common carrier activities. Section 2 is simply a declaration of purpose that the authority of the Commission applies in appropriate cases to communication by wire and in other cases to communication by radio, and by its terms is restricted to apply only to other "provisions of this Act." 47 U.S.C. 152(a).

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[17] S. Rep. No. 781, 73d Cong., 2d Sess. 1 (1934); H.R. Rep. No. 1850, 73d Cong., 2d Sess. 3 (1934); H.R. Rep. No. 1918, 73d Cong., 2d Sess., p. 47 (1934).

Conceding that CATV systems are not common carrier services, the Commission nonetheless maintains that "communication by wire" in Sections 1 and 2(a) of the Act, is not confined to common carriers. These sections, according to the Commission, are a separate and independent grant of authority to regulate non-common carrier wire communications which include CATV activities.

Under Section 2(a) of the Act the Commission does not have authority to regulate CATVs engaged in wire communication, since the explicit terms of Section 2(a) limit the Commission's authority to the "provisions of this Act" and the Act is without any such "provisions," substantive or procedural, or authority relating to wire communication by non-common carriers in general and CATV in particular.[18]

The absence of any such regulatory provisions relating to non-common carriers engaged in wire communications, when contrasted with the comprehensive regulatory regime governing radio and common carriers spelled out in detailed provisions implementing Section 2(a), reveals the purpose of the Act to regulate common carriers, but not to regulate non-common carriers engaged in wire communication.

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[18] The terms "wire communication" or "communication by wire" appear in a number of sections of the Act other than Sections 1 and 2(a). Thus one or the other term is used in a number of the provisions of Title II, however only in connection with common carriers. Moreover, the terms may also be found in Sections 2(b), 3(a), 3(e), 4(b), 4(k), 4(o), 406, 410(a), 412, 502, 503(a), 602(b), 602(d), 604(c), 605 and 606 of the Act, 47 U.S.C. Secs. 152(b), 153(a), 153(e), 154(b) 154(k), 154(o), 406, 410(a), 412, 502, 503(a), 602(b), 602(d), 604(c), 605, 606 (1964).

The legislative history of the Act expresses the intent to exclude from Commission regulatory authority non-common carrier wire communication. The statement of the managers on the part of the House, included in the Conference Report, noted that the Senate version of Section 3(h), 47 U.S.C. Sec. 153(h) (1964), had been adopted:

> It is to be noted that the definition does not include any person if not a common carrier in the ordinary sense of the term, *and therefore does not include press associations* or other organizations engaged in the business of collecting and distributing news services which may refuse to furnish to any person service which they are capable of furnishing, and may furnish service under varying arrangements, establishing the service to be rendered, the terms under which rendered, and the charges therefor. H.R. Rep. 1918, 73d Cong., 2d Sess. 45-46 (1934) (Emphasis added).

Thus, the draftsman deliberately excluded any wire communication other than common carriers outlined in Title II.

B. Title III Pertains to Radio Transmission, Rather Than Reception and Distribution by Cable, and Establishes a System of Licensing Regulation.

The method of regulation under Title III of the Act chosen by Congress is *licensing*. *Regents of the University of Georgia v. Carroll,* 338 U.S. 586 (1950). See also *Federal Communications Commission v. American Broadcasting Co.,* 347 U.S. 284, 289-290 (1954).

In *Southwestern Cable Co. v. United States,* 378 F. 2d 118 (9th Cir. 1967), *cert. granted* 389 U.S. 911 (1967), this Court examined the basis for the Commission's newly asserted jurisdiction over CATV and held that the "method of regulation of *broadcasting* chosen by Congress was licensing." Since petitioner here, as in *Southwestern,* is a CATV operator, and as such neither a licensee nor applicant for license, petitioner is beyond the ambit of the Commission's licensing authority and control. Commission attempts to regulate CATV other than by its licensing procedure are invalid. Since CATV systems seek no radio frequencies in their operations and are not before the Commission for license application, modification, or renewal, the Commission is without jurisdiction or authority to regulate them.

CATV operation is a reception service and not a transmission service. The whole thrust of the Radio Act of 1927 and Title III of the Communications Act of 1934 was to confer on the Federal Radio Commission and the FCC authority over transmission, but not over reception. Section 301 of the Communications Act, 47 U.S.C. 301, defining the scope of Title III of the Communications Act, makes this abundantly clear when it states:

> It is the purpose of this Act, among other things, to maintain the control of the United States over all the channels of interstate and foreign *radio transmission;* and to provide for the use of such channels, but not the ownership thereof, by persons for limited periods of time, under licenses granted by Federal authority . . . [Emphasis added.]

There is nothing in any of the specific statutory provisions cited by the Commission as the basis for its authority

which indicates that the Commission's Title III authority extended to anything but regulation of transmission. Sections 4(i) and 303(r) give the Commission broad rule making authority to carry out the provisions of the Act. But by themselves they confer no independent power; they are dependent upon other substantive provisions.

Section 303(f) authorizes the Commission to promulgate rules and regulations designed to prevent interference among stations. This section clearly relates to transmission alone. There is nothing whatsoever in the activities of CATV that directly or indirectly causes any interference among stations and the CATV rules do not relate to transmission interference. Section 303(h) authorizes the Commission to establish areas or zones to be served by stations. Again, the subject matter is clearly transmission.

The last "crucial" section relied upon by the Commission for regulatory power over CATV is Section 307(b). This section provides:

> In considering applications for licenses, and modifications and renewals thereof, when and insofar as there is demand for the same, the Commission shall make such distribution of licenses, frequencies, hours of operation, and of power among the several States and communities as to provide a fair, efficient, and equitable distribution of radio service to each of the same.

By its terms this section is limited to transmission and its method of regulation is by license, whether it be applications for licenses, modifications, or renewals. Section 307(b) provides that when conflicting demands exist for frequencies, the Commission is to make an equitable allocation.

The inconsistency of the Commission's present position and the over-reaching nature of its CATV jurisdictional grab is perhaps best illustrated by its conduct in 1962 in connection with the All-Channel Receiver Law. In 1962, the Commission sought and received Congressional legislation designed to allow the Commission to require UHF reception capability for all commercial television receivers. (47 U.S.C. 303(s), 330 (1962), H. Rep. No. 1559, S. Rep. No. 1525, 87th Cong., 2d Sess. (1962).)

The Commission recognized that its authority over reception devices was inadequate, and in requesting the All-Channel Receiver Law, it candidly stated to the Congress (Hearings on H.R. 8031 before the House Committee on Interstate and Foreign Commerce, 87th Cong., pp. 7-8 (1962)):

> In the Communications Act of 1934, Congress vested the Federal Communications Commission with the responsibility of making available to all people of the United States, an efficient and nationwide communications service, and certain authority to carry out these responsibilities. Our request for this legislation is an expression of our feeling that in the area of television reception systems, our present authority is not commensurate with our responsibilities . . . .

The Congress obviously agreed with the Commission as to lack of authority over reception for it proceeded to enact the All-Channel Receiver Law, which added to the Communications Act the only reference or application to radio reception.

There is no significant distinction between limitation on the use of individual *receiving* sets and the present attempted foreclosure or limitation on the use of various CATV receiving apparatus. The Commission was obviously right in 1962 in

asking Congress for a specific grant of authority to deal with the subject of reception. Its claim now under Title III of the Communications Act to deal with the subject of CATV is an outright usurpation of authority.

C. The Commission Lacks Any Statutory Standard to Regulate Non-Common Carrier Wire Communications

The Communications Act contains both general and detailed standards for the regulation of radio communication and common carriers. Radio licensing under Title III must be administered in the "public interest, convenience, or necessity." Similarly, regulation of common carriers under Title II must be in the "public convenience and necessity," 47 U.S.C. 214.[19] These general standards are given meaning and substance in numerous provisions of the Act dealing with substantive, procedural and remedial matters relating to the regulation of common carriers and radio communications. Those provisions incorporate the basic legislative standards governing the regulatory authority conferred on the Commission. They specify in detail the substantive and procedural criteria for

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[19] As explained in part I, these similar standards are given vastly different interpretations relating to the public interest considerations, protections, and rights under each regulatory category and problem.

regulation under Title II[20] and under Title III.[21]

The Act contains no such similar structure of substantive and procedural provisions for wire communication engaged in by non-common carriers. The general regulatory provisions relied upon by the Commission for its jurisdiction over CATV qualify the power granted with limitations such as "not inconsistent with this Act, as may be necessary in the execution of [the Commission's] *functions*" (Section 4(i));"not inconsistent with law as it may deem necessary . . . to carry out the *provisions* of this Act" (Section 303(f));"or as may be necessary to carry out the *provisions* of this Act" (Section 303(r), emphasis added). However, with respect to non-common carrier wire communication there are no "provisions of this Act"

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20 *E.g.*, unjust and unreasonable discriminations, 47 U.S.C. Sec. 202(a); the use of franks and passes, 47 U.S.C. Sec. 210(a); adequacy of facilities, extension of lines and public offices, 47 U.S.C. Sec. 214(d); required records and depreciation practices, 47 U.S.C. Sec. 220(a)(b); length of suspension of new charges, and hearing requirements, 47 U.S.C. Sec. 204; court injunction involving reductions or extensions of service, 47 U.S.C. Sec. 214(c); cease and desist authority, 47 U.S.C. Sec. 205(a); claims for damages in proceedings instituted either in the courts or before the Commission, 47 U.S.C. Secs. 206, 207, 208 and 209.

21 *E.g.*, classification of radio stations, including areas and zones served and power and time of operation, 47 U.S.C. Sec. 303; restrictions on grants to aliens, 47 U.S.C. Sec. 310; operation of transmitting apparatus by licensed operators, 47 U.S.C. Sec. 318; standards for distribution of licenses, frequencies, hours of operation and power among the several states and communities, 47 U.S.C. Sec. 307(b); terms of licenses and standards, as well as procedural requirements governing renewals, 47 U.S.C. Sec. 307(d); and substantive and procedural conditions governing modification, suspension and revocation of licenses, 47 U.S.C. Secs. 303(f), 303(m), 312 and 316.

or Commission "functions" defined elsewhere in the Communications Act to give meaning or limit to these general regulatory powers. And in the absence of any substantive and procedural authority or limitation, the Commission's argument is reduced to the contention that it has the jurisdiction to regulate CATV, *i.e.*, wire communication conducted by non-carriers, for whatever purposes and means it may consider appropriate.

A further difficulty with the Commission's position is that it chooses from only one of the multitude of objectives contained in the Act, some of which relate to radio communication and some of which relate to common carriers, to provide the required standards. The *First Report and Order* states that the Commission made the judgment that CATV should operate in a supplemental or auxiliary role to broadcasting and that the development of CATV should be limited by this objective. The explicit premise of the objective which it chose was to protect and insulate from competition the broadcast industry which it does have the power to regulate. On this theory, the Commission might have been equally free to choose entirely different objectives as the bases for regulation. Instead of protecting broadcasting against competition, it might have concluded with equal "validity" that the mandate of Section 307(b) of the Communications Act, which provides for a "fair, efficient and equitable distribution of radio service," requires that television broadcasting be curtailed and replaced by CATV in order to conserve valuable spectrum space. Alternately, the Commission could have with equal logic chosen to regulate CATV in such a manner as to supplement common carrier service but to curb any threat it may present to communication common carriers. The availability of such a wide choice of regulatory objectives amounts to no statutory standard whatsoever.

Even if it were possible to conclude that Sections 303(h) and 307(b) provide a substantive standard of some sort, no procedural standards whatsoever are provided for the regulation of non-common carrier wire communication. In the area of radio and common carrier regulation, procedural provisions of the Act operate to give meaning and assure procedural due process in the Commission's exercise of the delegated regulatory powers. To choose but two examples, radio stations licenses may be modified under Section 316 of the Act, but that provision requires a prior hearing on request. Similarly, the Commission is authorized under Section 214(d) of the Act to require a carrier to improve its service by providing adequate facilities, extending lines, etc. However, that provision requires a prior "full opportunity for hearing."

The complete absence of either procedural or substantive standards for the asserted authority to regulate CATV as a non-common carrier wire communication activity permits only one of two possible conclusions. The first is that even if Congress may have intended the Commission to exercise regulatory authority over such activity, the attempted delegation is invalid for lack of standards. *Panama Refining Co. v. Ryan*, 293 U.S. 388 (1935); *Schecter Poultry Corp. v. United States*, 295 U.S. 495 (1935).[22] The second is that the lack of standards evidences Congress' intent that such activities not be

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[22] It is recognized that these cases have been roundly condemned in their invalidation of important New Deal legislation for lack of adequate legislative standards. They have however been given some new life by the dissent of Justice Harlan in *Arizona v. California*, 373 U.S. 546, 625-626 (1963). Certainly, here they have added force where it is not the legislative standard fixed by Congress which is challenged, but the stretching of this standard by the administrative agency to embrace a wholly new class of persons under an entirely new scheme of regulatory control.

regulated. The latter conclusion is wholly consistent with the legislative history and structure of the Act.

D. An Administrative Ruling Recognized by the Courts and Acquiesced to by Congress Has the Force of Law and Cannot be Overturned by the Agency.

It is a well settled principle of statutory construction that a prior and consistent administrative interpretation is given great weight by the courts, *Norwegian Nitrogen Products Co. v. United States*, 288 U.S. 294, 313-315 (1933). Even greater weight is given to the administrative interpretation where Congress becomes aware and acquiesces to the construction of the statute as interpreted by the administrative agency. *United States v. Leslie Salt Co.*, 350 U.S. 383, 396-397 (1956), affirming the decision of this Court, 218 F. 2d 91 (9th Cir. 1954).

The conclusiveness of the original administrative interpretation is strengthened where the question is the scope and power of the agency to issue legislative rules, *United States v. American Trucking Association*, 310 U.S. 534, 549 (1940). It is likewise strengthened where the courts have recognized the prior administrative interpretation, *Corn Products Refining Co. v. Commissioner of Internal Revenue*, 350 U.S. 46, 53 (1955); *N.L.R.B. v. Gullet Gin Co.*, 340 U.S. 361, 365-366 (1951). But where the Congress is deemed to have approved the long-standing administrative interpretation by not amending or by re-enactment of the statute, the interpretation has the force and effect of law. *Helvering v. Winmill*, 305 U.S. 79, 83 (1938), cited with approval in *Fribourg Navigation Co. v. Commissioner of Internal Revenue*, 383 U.S. 272 at 283-284 (1966);

J. C. Boswell Company v. Commissioner of Internal Revenue, 302 F. 2d 682, 685 (9th Cir. 1962), *cert. denied* 371 U.S. 860 (1962).

Since 1958, the FCC had frequently and consistently held that it did not have regulatory jurisdiction over the operation of community antenna television systems either directly or through the microwave carrier. *Frontier Broadcasting Co. v. Collier,* 24 F.C.C. 251 (1958); *CATV and TV Repeater Services,* 26 F.C.C. 403 (1959); *WSTV, Inc. v. Fortnightly Corp.,* 23 Pike and Fischer R.R. 184 (1962). This absence of jurisdiction over CATV was judicially noticed by this Court in *Cable Vision, Inc. v. KUTV, Inc.,* 335 F. 2d 348 (9th Cir. 1964), *cert. denied,* 379 U.S. 989 (1965).

In an effort to acquire limited CATV jurisdiction the agency's want of jurisdiction was first brought to the attention of the 86th Congress along with certain legislative recommendations of the Commission, 105 Cong. Rec. 6753 (1959).[23] Lengthy hearings through the summer and fall of 1959 were held by a subcommittee of the Senate Committee on Interstate and Foreign Commerce on the legislation proposed by the FCC.[24] The full Senate Interstate and Foreign Commerce Committee then favorably reported a bill to grant the Commission jurisdiction to regulate community antenna systems in certain circumstances. S. Rep. No. 923, 86th Cong., 1st Sess.

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[23] For a legislative history of the Commission's unsuccessful attempts to get a jurisdiction grant from the Congress over CATV see Appendix A, p. 37a.

[24] *Hearings before the Communications Sub-Committee of the Committee on Interstate and Foreign Commerce, United States Senate,* 86th Cong., 1st Sess. (1959), *of VHF Booster and Community Antenna Legislation.*

(1959), accompanying Senate Bill 2653 entitled "A Bill to amend the Communications Act of 1934 to establish jurisdiction in the Federal Communications Commission over community antenna systems." In 1960, after several days of debate, the Senate recommitted the bill and no legislation authorizing FCC regulation of community antenna systems was enacted by the 86th Congress. 106 Cong. Rec. 10520, 10547 (1960).[25] Again, in 1961, the FCC submitted to the 87th Congress proposed legislation giving it jurisdiction to regulate community antenna systems. 107 Cong. Rec. 2523 (1961); S. 1044 and H.R. 6864, 87th Cong., 1st Sess. (1961). The 87th Congress similarly failed to enact any legislation conferring the Commission with jurisdiction over the community antenna industry.

Following these unsuccessful attempts to attain Congressional grant of jurisdiction, the Commission in a series of proceedings culminating in the *Second Report and Order,* 2 F.C.C. 2d 725 (1966) reversed its prior rulings and assumed regulatory control over CATV systems under its rule-making procedures. Thus, the Commission upset and reversed its prior holdings that it had no jurisdiction over CATV, which was then in its fifteenth year of operational history.

Uncertain of this bold usurpation of jurisdiction, the Commission again appealed to Congress for jurisdiction over CATV systems, House Report 1635, 89th Congress, 2nd Sess., submitted June 17, 1966 to accompany H.R. 13286. This bill failed to pass the Congress as did the prior attempts. By its assumption of jurisdiction, the Federal Communications Commission has erroneously attempted to reverse its prior decisions which, by court recognition and Congressional approval, had assumed the force and effect of law.

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[25] For extracts of the debate see Appendix B, pp. 43a-52a.

The Supreme Court has rarely departed from its doctrine of longstanding administrative interpretation. The arguments for departure are generally factual: that there is a doubt as to whether the administrative agency did in fact decide the matter, *Baltimore and Ohio Railway Company v. Jackson,* 353 U.S. 325, 330-331 (1957); that Congress did not clearly acquiesce to or approve the administrative ruling, *Cammarano v. United States,* 358 U.S. 498, 510-511 (1959); or that there was no approval since Congress had failed to focus on the issue, *Fribourg Navigation Co. v. Commissioner of Internal Revenue,* 383 U.S. 272, 283-284 (1966).

In the latter two cases the Court rejected the argument for departure on adverse findings. Here the agency passed upon its jurisdiction and found it had none. The Congress approved this ruling when it rejected the proposed amendment "to establish jurisdiction in the Federal Communications Commision over community antenna systems."

The FCC, created by Congress, performs rule-making functions designated by Congress. Its jurisdiction and purposes are set out in its controlling statute with great specificity. It has usurped jurisdiction, which it consistently held it did not possess, and which the Congress repeatedly failed to grant after a number of attempts. The Commission's prior administrative interpretation that it did not possess jurisdiction, recognized by the courts and acquiesced to and approved by the Congress, has the force and effect of law and cannot be overturned by a subsequent ruling by the Commission.

III.

The Non-Duplication Rules Restricting the Reception and Distribution of Television Signals Are in Violation of the First Amendment.

The Commission's non-duplication rules in Sections 21.712 and 74.1103, and its summary order against petitioner are a prior restraint in the reception and distribution of information and tread upon free speech guarantees of the First Amendment. The non-duplication rules provide that the CATV system, upon request of the local television station, will black out same-day imported signals which duplicate local signals.

Respondents have stoutly maintained that the enforcement of the non-duplication rules eliminates no programming or the public's access to information, but merely the duplication of program materials already available to allow the local stations a competitive advantage. This argument does not conform to the facts in Great Falls, Montana. The principal service which petitioner markets is the availability of programs at times different from the exhibition of the same program by the local stations. Petitioner has voluntarily agreed to give simultaneous non-duplication protection, but the rule requires and respondents insist upon same-day non-duplication. Same-day non-duplication very immediately limits the access of the public to information and materials at the *times available to the viewer.* Furthermore, non-duplication eliminates public access to all but one of competing programs broadcast simultaneously by the local stations. Limiting petitioner's distribution of news, information, and program materials otherwise available by cable television is an unreasonable restriction

upon the exercise of free speech in violation of the First Amendment.

"The right of freedom of speech and press includes not only the right to utter or to print, but the right to distribute [and] the right to receive . . ." *Griswold v. Connecticut,* 381 U.S. 479, 482 (1965). Communication by any lawful means – motion picture, radio, television, newspaper, closed-circuit, hand-bill, the mails, etc. – falls within the constitutional protections provided by the First Amendment. *ABC v. United States,* 110 F. Supp. 374 (SD NY, 1953), aff'd *sub nom. Federal Communications Commission v. ABC,* 347 U.S. 284 (1954); *Weaver v. Jordan,* 64 Cal. 2d 235, 411 P. 2d 289 (1966), *cert. denied,* 385 U.S. 844 (1966).

The entire stream of communications from source to destination is constitutionally protected. This fundamental constitutional principle embraces not only the right of publication but also the rights of dissemination and distribution, as well as of reception. *Saia v. New York,* 334 U.S. 558 (1948); *Winters v. New York,* 333 U.S. 507 (1948); *Martin v. Struthers,* 319 U.S. 141 (1943). Circulation is equally protected. "Liberty of circulating is as essential to that freedom [freedom of press and speech] as liberty of publishing; indeed, without the circulation, the publication would be of little value." *Ex Parte Jackson,* 96 U.S. 727, 733 (1877); *Lovell v. City of Griffin,* 303 U.S. 444 (1938).

Once established that the communication or medium is constitutionally protected, the government shall impose no prior restraints or condition upon the free exercise of a benefit or privilege if the effect thereof is to "inhibit or deter the exercise of First Amendment freedoms." *Sherbert v. Verner,* 374 U.S. 398, 404-405 (1963); and see *LaMont v. Postmaster General,* 381 U.S. 301 (1965).

The primary purpose of the First Amendment, as it relates to speech and press, is to suppress prior restraints upon publication, circulation or distribution. *Joseph Burstyn, Inc. v. Wilson*, 343 U.S. 495 (1952). With "respect to the vital importance of protecting this essential liberty from every sort of infringement" (*Lovell v. City of Griffin, supra*, at p. 452); see *Near v. Minnesota*, 238 U.S. 697 (1931); *Grossjean v. American Press Company, Inc.*, 297 U.S. 233; *DeJonge v. Oregon*, 299 U.S. 353 (1937). Freedoms [guaranteed by the First Amendment] . . . are protected not only against heavy-handed frontal attack, but also from being stifled by more subtle governmental interference." *Bates v. City of Little Rock*, 361 U.S. 510, 523 (1960).

Particularly objectionable is the practice of censorship exercised through the vehicle of licensing authority. "The struggle for the freedom of the press was primarily directly against the power of the licensor." *Lovell v. City of Griffin, supra*, at p. 451. See also the Chief Justice's dissent in *Times Film Corporation v. Chicago*, 365 U.S. 43 (1961). Indeed, any "intimidation" by the government upon *distribution* of constitutionally protected material, no matter what the purpose, is hostile to the mandate contained in the First Amendment and must be terminated forthwith. *Bantam Books v. Sullivan*, 372 U.S. 58, 70 (1963).

In the field of radio and television communications the only permissible restraint has been related to the physical limitation of available frequencies in the spectrum. In *NBC v. United States*, 319 U.S. 190 (1943), the Supreme Court held that *because of limitation of available frequencies* reasonable regulation under the licensing standard of public convenience and necessity is neither a violation of the First Amendment nor is it censorship within the meaning of Section 326 of the Communications Act, 47 U.S.C. 326. In another radio licensing case, *Lafayette Radio Electronics Corp. v. Federal Communications Commission*, 345 F. 2d 278 (2d Cir., 1965), the court there upheld the Commission's restrictions on the permissible nature of radio transmissions using the Citizen's Band Radio Service *because of natural limitations in available frequencies.*

In preserving scarce frequency space the Commission through its licensing promoted the exercise of free speech, since if everyone were to broadcast no one could be heard. Commission reliance on *NBC* and *Lafayette* as authority for prior restraint of CATV carriage is misplaced, since CATV occupies no frequency space. Unlike the broadcast licensing rules, the non-duplication rules do not promote free speech and are unreasonable.

Carter Mountain Transmission Corp. v. Federal Communications Commission, 321 F. 2d 359 (D.C. Cir., 1963), *cert. denied*, 375 U.S. 951 (1963), upheld a denial of a radio license to a common carrier for microwave service to a CATV system. The court there side-stepped the First Amendment question and held that this was a "licensing" procedure and not regulation of CATV. Moreover, the court pointed out that the CATV system was not a party to the case and neither its rights nor those of its subscribers were before the court. See also *Idaho Microwave, Inc. v. Federal Communications Commission*, 352 F. 2d 729 (D.C. Cir., 1965) where the CATV system was before the court as intervenor in the licensing of radio microwave transmission to a CATV system. There the court met First Amendment objections by explaining that it was concerned with "licensing" of microwave radio and not regulation of CATV or its rights to receive and distribute.

Thus, while under the accepted system of radio licensing, applicants have been denied a license for a radio station without impairment of First-Amendment freedom, there is no precedent supporting FCC's proscription on distribution of communications over closed-circuit cable facilities for which no federal license is required. And the FCC cannot lawfully condition the public's guaranteed access to common carrier services upon relinquishment of the constitutional right to distribute or receive free of governmental restraint.

Although the First Amendment argument was raised before this Court in *Southwestern Cable Co. v. United States*,

378 F. 2d 118 (9th Cir. 1967), *cert. granted,* 389 U.S. 911 (1967), it was not passed upon by the Court, and since that case did not involve non-duplication the argument was not reasserted in the Supreme Court.

"Congress has from the first emphatically forbidden the [Federal Communications] Commission to exercise any power of censorship over radio communications." *Farmers' Union v. WDAY,* 360 U.S. 525, 529 (1958). Section 326 of the Communications Act (47 U.S.C. 326), which *limits* the jurisdiction and authority of the administrative agency, reads in full as follows:

> Nothing in this Act shall be understood or construed to give the Commission the power of censorship over the radio communications or signals transmitted by any radio station, and no regulation or condition shall be promulgated or fixed by the Commission which shall interfere with the right of free speech by means of radio communication.

Without equivocation, therefore, the Congress has prescribed that the FCC shall promulgate no regulation or *condition* which may be understood, construed or used to infringe upon or interfere with the right of free speech, nor shall the Commission be empowered to take any action constituting censorship over radio communications or over *"signals transmitted by any radio station."*

Here the Commission is repressing maximum distribution of communications made possible by technical advances. Petitioner has sought to demonstrate that its operation and distribution are not harmful to local television. Under these circumstances there is no reasonable protection of the public interest which warrants a restriction on petitioner's First

Amendment rights to freely distribute available television signals. Accordingly, the Commission's non-duplication rule and its proscriptive order halting a substantial part of petitioner's distribution without reference to any reasonable public interest is an unlawful restriction of the freedom of speech in violation of the First Amendment.

IV.

Failure to Provide for an Evidentiary Hearing in Modifying Petitioner's Business Is in Violation of the Due Process Clause and Pertinent Statutes.

The Federal Communications Commission does not purport to license CATV, but it assumes a greater restrictive and discriminatory control over CATV than exercised over any other communications medium. The Commission's CATV rules are admittedly protective of the preferred broadcaster, restrictive of free competition, and deny minimum safeguards of a fair hearing as required by the Fifth Amendment, the Administrative Procedure Act, the Communications Act of 1934, and the Commission's own rules for licensing, as guaranteed to all other communications media over which the Commission exercises regulatory control.

Petitioner's affiliate and intervenor here, TelePrompTer Transmission of Kansas, originally instigated these proceedings in 1965 for modification of its existing license to add radio FM signals to its service to the Great Falls CATV system. No hearing was sought at that time. In 1965 petitioner was not subject to direct FCC regulatory control. Upon promulgation of the *Second Report and Order* in 1966 petitioner intervened in the proceeding also seeking waiver of the non-duplication rules. Again no hearing was asked. However,

petitioner and intervenor had no forewarning that on a waiver petition the Commission would issue a proscriptive order compelling compliance within thirty days of issuance, foreclosing a substantial part of petitioner's service and causing almost certain destruction of its business. Nor did petitioner know that the Commission would reject out of hand uncontroverted, verified, factual allegations of destruction of its business contained in its pleadings and make unsupported findings in conflict with the allegations.[26] As a recourse, petitioner could have petitioned the Commission to reconsider its order and at that time sought a hearing. However, the Commission in other such cases has denied any relief during the pendency of the motion for reconsideration, forestalled the motion for as much as a year precluding interim relief in appeal, and then summarily reaffirmed its prior denial. In view of this Commission policy, petitioner has instead moved in this Court. To have sought a hearing would have been idle since the Commission has granted none in similar circumstances. Petitioner's failure to have sought a hearing should not foreclose its constitutional rights of due process in the taking and destroying of its business. Constitutional rights and due process are not to be so easily foreclosed. Moreover, since the rules fail to provide for hearing by right, petitioner cannot be said to have waived a right which the rules withheld.

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[26] The *First Report and Order* concludes that non-duplication "need impose no substantial burden on the ordinary CATV operator or his subscribers," 38 FCC at 714, para. 79, and should the rules prove unduly burdensome, "special action or waiver can be obtained upon an appropriate showing." *Id.* at 715, para. 82. The promised relief was denied here.

A. The Issuance of a Summary Order by an Administrative Agency Threatening Property Rights is a Denial of Due Process in Violation of the Fifth Amendment.

In the absence of a hearing, the issuance of a proscriptive order halting a substantial part of petitioner's business is a deprivation of property without due process of law in violation of the Fifth Amendment. When administrative agencies make binding determinations affecting the legal rights of individuals, "it is imperative that those agencies use the procedures which have traditionally been associated with the judicial process." *Hannah v. Larche,* 363 U.S. 420 at 442 (1960).

Modification of a certificate of convenience without hearing raises due process implications. *CAB v. Delta Air Lines,* 367 U.S. 316, 330 (1961), citing *Seatrain Lines v. United States,* 64 F. Supp. 156 at 161 (D. Del. 1946), affirmed 329 U.S. 424 (1947). *Seatrain* held that the ICC could not alter or cancel an original certificate given to a water carrier. The lower court had held the Commission's order would deprive Seatrain of property without due process of law in violation of the Fifth Amendment, 64 F. Supp. 156 at 161. In affirming the Supreme Court noted that *Seatrain* had been conferred "grandfather" rights, as here, and in reliance had expended large sums in its business, which the order would have threatened.

In *Superior Oil Company v. F. P. C.,* 322 F. 2d 601 (9th Cir. 1963), *cert. denied,* 377 U.S. 922 (1964), this Court examined due process issues concerning a denial of hearing in an administrative proceeding and observed that in *United States v. Storer Broadcasting Co.,* 351 U.S. 192 (1956) due process was not raised. The Court held that due process

required governmental agencies in adjudications to observe the traditional judicial processes, citing *Hannah v. Larche, supra.*

More recently in *Southwestern Cable Co. v. United States,* 378 F. 2d 118 (9th Cir. 1967), *cert. granted,* 389 U.S. 911 (1967), Judge Ely in his concurring opinion reasoned that the petitioner had relied upon the Commission's previous disavowal of jurisdiction over CATV in investing substantial sums of money. The Commission's proscriptive order, if enforced, would adversely affect, if not destroy, the petitioner's investments. In light of this, Judge Ely stated that "the Commission trespassed upon constitutional safeguards against the confiscation of property." Here, the Commission's order is not merely a freeze or a maintenance of the *status quo* as it was in *Southwestern,* but it threatens destruction of petitioner's entire business.

Standard Airlines, Inc. v. Civil Aeronautics Board, 177 F. 2d 18 (D.C. Cir. 1949) held that a regulatory agency could not create a special class of irregular carrier by granting "letters of registration" with the right to revoke it at any time rather than a certificate of public convenience, in an attempt to circumvent a hearing on revocation or alteration of rights. The court explained:

> The controlling practicality, in our view, is that the suspension would destroy property, not a license property but investment and business property. The Government cannot make a business dependent upon a permit and make an otherwise unconstitutional requirement a condition to the permit. (177 F. 2d at 20.)

Here the same device has been employed against the petitioner and other CATV operators who are not license holders. Yet,

the Commission, in its "special regulatory control" over CATV business, seeks to alter and destroy petitioner's business by proscriptive order without permitting the elementary safeguards of due process as provided by the Fifth Amendment.

Gonzales v. Freeman, 334 F. 2d 570 (D.C. Cir. 1964), dealt with due process aspects in summary suspension of the privilege of contracting with the government. In reversing the agency's action, the court explained that there was no right to contract with the government, but that the suspension of the privilege involved severe *economic injury.* Such circumstances called for application of basic principles of fairness and *due process.* In applying these principles, the court offered these guidelines: How was the individual to be hurt? What governmental interest was to be protected? How would the governmental interest be affected, if at all, by extending procedural safeguards to cover the challenged action?

Applying these principles to the instant case: petitioner is faced with destruction of its entire investment; the admitted governmental interest is protection of local broadcasting which has failed to demonstrate or even allege harm; as to the extending of procedural safeguards, the government has no business broadening its jurisdiction over a new class to convey new rights to a favored, vested class, when it cannot guarantee the ordinary minimum safeguards of due process and fair play.[27]

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[27] The Commission claims that it cannot guarantee a hearing in waiver petitions since hearings for the 1800 systems would impede the orderly working processes of the Commission. This argument is somewhat spurious in light of Rule 74.1107 (a), which requires an evidentiary hearing for new service in the top 100 markets on the bear objection by a local station. Before commencement of the new service, there must be an affirmative showing by the CATV system

(continued)

In its summary action and conclusionary findings the Commission has demonstrated a callous disregard of fair play and due process. In its failure to provide for a hearing it has barred consideration of the harm likely to be suffered. It has stuck steadfastly to its general preconceptions favoring television by eliminating competition whether or not the competition has any decided impact on the preferred television, and it has ignored the factor of fair play in the issuance of its proscriptive order. The Commission action has threatened the property and investments of petitioner's six year business, established in reliance upon the Commission's licensing of common carrier microwave service to furnish undiluted programming to petitioner's business, and incurred in the period the Commission steadfastly maintained it had no jurisdiction over CATV. The Commission's rules in failing to provide for hearing in the issuance of proscriptive orders threatening destruction and economic injury are in violation of due process guarantees of the Fifth Amendment.

B. Pertinent Statutes and Regulations Require a Hearing Prior to Modification or Revocation of an Existing Business.

The conduct and requirements for adjudication and rule making by government agencies are subject to the provisions of the Administrative Procedure Act, 5 U.S.C. 551 *et seq.* The Act

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27 (continued)

that its proposed service would not adversely affect local TV. Mere hearing delay can break the back of a new operator. Thus, the Commission compels a hearing when it will serve broadcast interests, and denies a hearing where it will also serve broadcast interests. Due process and the orderly functioning of the Commission are mere incidental considerations.

provides that "adjudication" shall be determined on the record after opportunity for agency hearing (5 U.S.C. 554) with the full safeguards of an impartial hearing examiner, the submission of evidence, right to subpoena witnesses, presentation of documentary evidence, transcript of record, preparation of findings and decisions (5 U.S.C. 556 and 557).

The Communications Act of 1934, 47 U.S.C. 151 *et seq.*, contains similar safeguards for administrative hearings affecting the rights of parties. The Act provides for a full evidentiary hearing for application for license where there exists a substantial and material issue of fact, 47 U.S.C. 309(e) and for full hearing for suspension of an existing license, 47 U.S.C. 303(m)(2). Before revoking a license or permit, the Commission must serve a show cause order and allow a party a full hearing, where the *burden of proof is upon the Commission*, 47 U.S.C. 312(c) and (d). Moreover, even a modification of license or construction permit entitles a party to full evidentiary hearing with the burden of proof placed upon the Commission, 47 U.S.C. 316. See *Civil Aeronautics Board v. Delta Air Lines*, 367 U.S. 316 (1961), concerning a modification of a certificate of convenience in violation of Section 401(g) of the Federal Aviation Act of 1958, 49 U.S.C. 1371(g).

In implementing the Communications Act and the requirements of the Administrative Procedure Act,the Commission's rules similarly provide for hearing: on the suspension of an operator license, 47 C.F.R. 1.85; on the modification of a radio license, 47 C.F.R. 1.87; and on revocation or in cease and desist proceedings, 47 C.F.R. 1.91. Without such minimum and traditional safeguards, individuals have no protection against arbitrary, capricious, or erroneous rulings and orders by quasi-judicial and administrative agencies.

Turning to the rules of conduct and operation pertaining to CATV, the Commission has initially drafted its regulations with the presumption or taint that CATV operation is "unfair" and adverse to the "public interest." *First Report and Order,* 38 F.C.C. 683, 713 (1965).

Sections 21.712 and 74.1103 require all CATV systems to carry local television station signals, and upon the request of the local station, black-out signals that duplicate local programs, Sections 21.712(g) and 74.1103(e). The rules permit a petition for waiver, Section 74.1109, but in acting on waiver petitions the Commission may summarily grant or deny the petition or specify other procedures, including oral argument or full evidentiary hearing, Section 74.1109(f). In short, under its new CATV rules, the Commission may treat the existing CATV system and its petition for waiver in any manner it chooses and subject it to any procedure it may arbitrarily select under the amorphous umbrella of "consistent with the public interest." Since it appears before the Commission with the taint that its operations are adverse to the public interest, the CATV system must overcome this presumption before gaining the relief sought, which, in consequence, shifts the burden of proof, contrary to the APA and the Communications Act. Thus far, the Commission has shown little inclination to listen to individual petitions and why its general rules should not apply in a particular circumstance.

Although the Commission did not initially license or otherwise authorize the existing operation of petitioner's CATV service, the Commission now seeks to exercise complete licensing authority over petitioner's business, while relegating it to "second class" business status. Without any statutory licensing standard for reasonable protection of market allocation of CATV, the Commission, by its new rules has created a special class of licensee. It has effectively placed CATV

operators under its vast powers and authority in dictating which, if any, services can continue to be furnished over cable facilities, yet at the same time, denying the traditional safeguards and protections guaranteed to all licensees.

The practice of creating a special class over which the administrative body seeks greater regulatory control was condemned in *Standard Airlines, Inc. v. Civil Aeronautics Board,* 177 F. 2d 18 (D.C. Cir. 1949). The same device is employed here where the Commission "confers" grandfather rights over an existing industry where previously it had held it had no jurisdiction; then attaches to it a tainted business category of unfair competition; and proceeds by its special regulatory edicts to destroy large portions of the industry, while denying any hearings or minimum safeguards allowed to all licensees and the favored groups protected by its new rules. See also this Court's opinion in *Southwestern Cable Co. v. United States,* 378 F. 2d 118 (9th Cir. 1967), *cert. granted,* 389 U.S. 911(1967), which held that the Commission's power to make rules was limited to its "licensing authority."

The Commission's order forcing petitioner to insure exclusivity within thirty days is proscriptive in nature and tantamount to a cease and desist order under Section 312 of the Act, 47 U.S.C. 312. Similar summary action by the Commission operating under the new CATV rules has recently been condemned and reversed by this Court in *Southwestern Cable Co. v. United States,* 378 F. 2d 118 (9th Cir., 1967), *cert. granted,* 389 U.S. 911 (1967). In that case the Commission ordered a freeze on the expansion of a CATV system carrying Los Angeles television stations into the San Diego area while it investigated the effect of such carriage. In its petition for review the CATV system challenged the Commission's authority to issue such an order and at the same time

broadly attacked the Commission's power and authority over CATV and the constitutional validity of its *Second Report and Order,* 2 F.C.C. 2d 725 (1966).

In response, the Commission contended that its action was not a cease and desist order under 47 U.S.C. 312, but was a grant of temporary relief under Section 74.1109(f), which, in turn, it claimed, was an exercise of its rule making authority under Sections 4(i) and 303(r) of the Communications Act, 47 U.S.C. 154(i) and 303(r). The Court rejected this argument pointing out that the order was prohibitory in nature and thus amounted to a cease and desist order, and that the Commission could not circumvent the safeguards of 47 U.S.C. 312 by misapplication of its rule making authority. In his careful opinion, Judge Barnes explained that "the method of regulation of broadcasting chosen by Congress was *licensing*" and "4(i) and 303(r) are limited to the scope of the Commission's *licensing authority.*" The Court concluded that as against a *non-licensee,* the Commission's only authority to issue proscriptive orders was limited to action under 47 U.S.C. 312, with the safeguards of a full adjudicatory hearing as provided in that section.

Here the Commission's action is even more proscriptive in nature than in *Southwestern,* since petitioner is ordered not just to maintain the *status quo,* but to cease and desist from operating an existing part of its business, maintained for over six years. As in *Southwestern, supra,* such an order must fail because it was issued without the minimum safeguards provided by Congress under Section 312.

The new CATV rules are in startling conflict with the requirements of the Administrative Procedure Act, the Communications Act, and the Commission's own rules in other areas of direct control and regulation. The CATV operations and the application of the new rules fall squarely within the problems

and procedures outlined in the Administrative Procedure Act. The Commission's order in the instant case represents "final disposition"[28] and affirmatively orders compliance as contained in 5 U.S.C. 551(6) and formulation of this order is an "adjudication" as defined in 5 U.S.C. 551(7).[29] Pursuant to 5 U.S.C. 554, petitioner is entitled to a full hearing.

The provisions of Section 9 of the Administrative Procedure Act, 5 U.S.C. 558, protect licensees of agencies against any "withdrawal, suspension, revocation, or annulment of any license" without a full evidentiary hearing. And Section 2(e) of the Administrative Procedure Act, 5 U.S.C. 551(8), defines "license," among other things, to include any "form of permission."[30]

Notwithstanding the statutory and regulatory requirements, as a matter of elementary fairness, it would seem that the Commission should give, at minimum, the same protections and safeguards to the CATV industry, over which it assumes inferential control, as it allows to the broadcasting industry, over which it has direct statutory licensing control.

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28 " '[O]rder' means the whole or a part of a final disposition, whether affirmative, negative, injunctive, or declaratory in form, of an agency in a matter other than rule making but including licensing." (5 U.S.C. 551(6)).

29 "[A]djudication" means agency process for the formulation of an order." (5 U.S.C. 551(7)).

30 " '[L]icense' includes the whole or part of any agency permit, certificate, approval, registration, charter, membership, statutory exemption or other form of permission." (5 U.S.C. 151(8)) " 'Licensing' includes agency process respecting the grant, renewal, denial, revocation, suspension, annulment, withdrawal, limitation, amendment, modification, or conditioning of a license." (5 U.S.C. 551(9)).

Section 309 of the Communications Act of 1934, 47 U.S.C. 309, provides for certain standards in granting of applications for licenses. The initial standard by which all applications are to be judged is a finding by the Commission of whether a public interest, convenience, and necessity will be served by the grantings of such applications. Subsection (e) of 309 provides that when a "substantial and material question of fact is presented" or the Commission for any reason is unable to make the finding of public interest, the Commission shall formally designate the application for hearing in which all interested parties may participate. See *Ashbacker Radio Co. v. Federal Communications Commission*, 326 U.S. 327 (1945); *Folkways Broadcasting Co. v. Federal Communications Commission,* 375 F. 2d 299 (D.C. Cir. 1967). The same considerations, which require the Commission to examine substantial and material issues of fact in determining the public interest for the grant of licenses, also require an examination of substantial and material issues of fact in a waiver petition.

Petitioner's verified petition for waiver of Sections 21.712 and 74.1103 of the Commission's rules[31] contains substantial and material factual issues warranting a hearing.

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[31] Under the Commission's rule of practice, 47 C.F.R. 1.52, the attorney's signature "constitutes a certificate by him that he has read the document; that to the best of his knowledge, information and belief there is good ground to support it; and that it is not interposed for delay." The waiver petition was not only signed by petitioner's attorney, but contained also a sworn affidavit of verification by the officer of petitioner most familiar with the facts and circumstances of the case.

At heart is petitioner's statement that program exclusivity will destroy its only marketable feature and cause the demise of the system. (Para. 15, of the FCC Order, R. p. 67). Additionally, petitioner alleged that there was no corresponding injury to local stations without providing program exclusivity. Despite the uncontroverted verified allegation, the Commission rejected petitioner's statement and concluded as a matter of fact disruption of CATV is minimized by its ruling. (Order, para. 16, R. p. 68). As to the absence of corresponding injury, the Commission ruled that "a broadcaster need not show specific injury." (Para. 16, R. p. 68). Here the broadcaster failed to show *any* injury.

Thus, the Commission has demonstrated that although it had provided for waiver of the rules and an evidentiary hearing in Section 74.1109, it did not intend in any case to vary from its factual, as well as legal, preconceptions contained in the *Second Report and Order.* Any attempts to show that these factual preconceptions did not conform to local conditions would not be tolerated. The entire basis for the exclusivity rules, the Commission explained, was the adverse impact that CATV might have on the growth of local television and the splintering or fractionalizing of its audience. Yet, the Commission, callously, if candidly, states that it is not concerned whether there is in fact an injury to the broadcaster.

Interstate Broadcasting Company v. Federal Communications Commission, 323 F. 2d 797 (D.C. Cir. 1963) reversed the Commission's action in denying an application for license without a hearing. The court held that, although under the "Storer doctrine" an applicant is not absolutely entitled to a hearing, in rejecting a hearing the Commission must make definite findings and adequately explain its conclusions and support them with specific findings of fact. The D.C. Circuit

cited its earlier opinions in *Television Corp. of Mich., Inc. v. Federal Communications Commission*, 294 F. 2d 730, 733 (D.C. Cir. 1961), where the court found a bare assertion by the Commission that its action was "clearly in the public interest," an inadequate explanation to support its order; and *Telanserphone, Inc. v. Federal Communications Commission*, 231 F. 2d 732, 735 (D.C. Cir. 1956), which reversed a Commission order because the conclusions were not adequately supported by a record for review. See also *American Trucking Association v. Federal Communications Commission*, 377 F. 2d 121 at 134 (D.C. Cir. 1967), *cert. denied,* 386 U.S. 943 (1967). The Commission's broad conclusions lack adequate factual support.

In *Civil Aeronautics Board v. Delta Air Lines*, 367 U.S. 316 (1961), the Supreme Court stressed that financial impact on an existing business was a critical issue for careful examination through a full evidentiary hearing. Similarly, *Folkways Broadcasting Co. v. Federal Communications Commission*, 375 F. 2d 299 (D.C. Cir. 1967), in reversing the denial of a hearing on a television application, held that economic impact and possible destruction of an existing station by a grant of a license required the Commission to conduct a hearing under 47 U.S.C. 309. Here also economic impact is a principal issue and the Commission has improperly failed to conduct a hearing before issuing its proscriptive order. If the Commission intended to make factual decisions adverse to the uncontroverted evidence in the pleadings, it was required to do so, only after an adjudicatory hearing and a ruling on the evidence presented.

For denial of petitioner's right to hearing, respondents rely principally on *United States v. Storer Broadcasting Co.*,

351 U.S. 192 (1956); *Federal Power Commission v. Texaco,* 377 U.S. 33 (1964); and *American Airlines, Inc. v. Civil Aeronautics Board,* 359 F. 2d 624 (D.C. Cir. 1966). This reliance is misplaced for none of these cases condoned proscriptive action against non-licensees in a waiver proceeding.

Here, the Commission has issued in a waiver procedure a proscriptive order against a non-licensee forecasting almost certain destruction of its existing business. The Commission's action and order exceeded its statutory and regulatory authority. Petitioner in its waiver petition is entitled to a hearing in the adjudication of its rights. *United States v. Storer Broadcasting Co., supra,* and *Federal Power Commission v. Texaco, supra.*

V.

The Non-Duplication Rules Are an Unreasonable and Arbitrary Restriction in Restraint of Trade Beyond the Legislative Purposes of the Communications Act.

Indisputably the Federal Communications Commission has broad regulatory power over matters within its subject jurisdiction. However, the administrative agency has no greater power than has been conferred by Congress. *Regents of the University System of Georgia v. Carroll,* 338 U.S. 586, 594 (1950); and the scope of this power is subject to judicial review, *Columbia Broadcasting System, Inc. v. United States,* 316 U.S. 407 (1942); *Stark v. Wickard,* 321 U.S. 288 (1944). Judicial review includes a determination of whether regulations promulgated by the agency are reasonably necessary and fairly appropriate for the legislative scheme. *American Trucking Associations, Inc. v. United States,* 344 U.S. 298 at 314-315

(1953). Although the court is not to supplant its judgment or discretion for that of the administrative agency, the regulations must bear a reasonable relation to the statutory purpose and must not be otherwise arbitrary. *Thompson v. Consolidated Gas Utilities Corp.*,300 U.S. 55, 69-70 (1937).

The administrative agency has wide latitude in the formulation of its regulations, and the courts will not interfere except "where the remedy selected has no reasonable relation to the unlawful practices found to exist." *Jacob Siegel Co. v. Federal Trade Commission,* 327 U.S. 608, 612-613 (1946). "Congress did not purport to transfer its legislative power to the unbounded discretion of the legislative body." *Federal Communications Commission v. Radio Corporation of America Communications, Inc.*,346 U.S. 86, 90 (1953). The exercise must be rational and within the bounds expressed by the legislative standard. *Burlington Truck Lines, Inc. v. United States,* 371 U.S. 156, 166-169 (1962).

Here, it will be shown that the Commission's CATV rules are built upon erroneous premises, are protective of a favored class of licensee, unfairly and unreasonably restrain legitimate competition of CATV to broadcasters, and bear no reasonable relationship to the purposes sought to be achieved. They are arbitrary, unreasonable and unnecessary restrictions against a new communications medium in protection of a favored, vested class.

A. The Regulation of CATV Duplication to Confer a Competitive Advantage to Broadcasting Is an Unreasonable and Arbitrary Restraint on Competition.

In its *First Report and Order,* 38 F.C.C. 683 (1965), the Commission explains its fundamental statutory responsibilities and policy are: to make available to all the people of the United States television service (47 U.S.C. 151); to encourage the larger and effective use of radio and television frequencies (47 U.S.C. 303(g)); and to distribute licenses and make a fair and equitable distribution of radio service throughout the United States (47 U.S.C. 303(b)). 38 F.C.C. at 697, para. 40. In accordance with this responsibility, it has designed a national scheme of frequency allocation, which is set forth in 47 C.F.R. 73.603. *Ibid.*, para. 41.

CATV, the Commission explains, can aid in carrying out this Commission allocation policy, *Id.* at 699, para. 44, but it may upset the policy by failing to carry local stations, *Id.* at 702, para. 50, or it may compete with local broadcasting in upsetting regional exclusivity provisions in the local station's contracts with network programs by importation and duplication of local programs, *Id.* at 703, para. 52-53. From these observations, the Commission concludes: (1) that the failure to carry local stations is inconsistent with CATV's *supplementary* role and contrary to the public interest; (2) that its unequal footing with broadcasters renders it an *unfair method of competition;* and (3) that the requirements of non-duplication and local carriage are not inconsistent with CATV's supplemental role. *Id.* at 705-706, para. 57.

From these findings and conclusions, the Commission has determined: (1) that every station is entitled to carriage and non-duplication by CATV, *Id.* at 713, para. 76; (2) that local

carriage and non-duplication are required "in order to ameliorate the adverse impact of CATV competition upon local stations, existing and potential," *Id.* at 713, para. 77; and (3) that local carriage and non-duplication requirements "need impose no substantial burden on the ordinary CATV operator or his subscribers" and be imposed "without unduly burdening or obstructing the operations of CATV systems," *Id.* at 714-715, paras. 79 and 81. In the event they should prove unduly burdensome, the Commission promised special action or waiver upon an appropriate showing. *Id.* at 715, para. 82. These findings and conclusions are endorsed and reaffirmed in the *Second Report and Order,* 2 F.C.C. 2d 725 at 778, paras. 131-133 (1966).

In sum, the Commission has cast CATV in a "supplementary role" to television broadcasting, branded it as "unfair competition," and embarked upon an unprecedented course of economic restriction and program control to protect the favored broadcast licensee. Commissioner Loevinger dissented from this new role of economic regulation for the Commission, and suggested that "expansion of service is not to be attained by the limitation of competition and the imposition of rigorous regulation but rather by stimulating competition and moderating regulation." *Id.* 746 at 759.[32]

By initiating economic regulation over CATV, the Commission has acted in absolute conflict with its opinion in *CATV and TV Repeater Services,* 26 F.C.C. 403 (1959), where it held that economic regulation over CATV in favor of broadcasters was "absurd." *Id.* at 432:

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[32] The dissenting opinion is quoted in full, Appendix A, p. 10a.

> In essence, the broadcaster's position shakes down to the fundamental proposition that they wish us to regulate in a manner favorable toward them vis-a-vis any non-broadcast competitive enterprise, . . . as closed-circuit music and news services, closed-circuit theatre television operators, and, possibly, even ordinary motion picture and legitimate stage operators, magazine and newspaper publishers, etc., comprising all of the entities which compete with broadcasting for the time and attention of potential viewers and listeners. *The logical absurdity of such a position requires no elaboration.* [Emphasis added.] (26 F.C.C. at 431).[33]

The interest of the Congress in maintaining free competition in the field of radio broadcasting is manifested in Section 314 of the Act, 47 U.S.C. 314, which prohibits those in the business of transmitting and receiving communications or signals by radio from any action which may substantially lessen competition or restrain commerce or unlawfully create a monopoly in any line of commerce. Section 313 of the Act, 47 U.S.C. 313, revokes the license of violators of the anti-trust laws.

The Communications Act regulates radio transmission principally in the interest of preserving rare spectrum space. This regulatory control marks the FCC and radio broadcasting from other regulatory agencies and their regulated industries. For instance, radio differs substantially from most transportation industries where competition under the controlling

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[33] For a more complete quotation from this opinion, see Appendix A, pp. 4a-9a.

statute has been deemed in certain circumstances to be adverse to the public interest. It is the principal function of the transportation agencies to set and control rates and to determine what degree of competition is necessary and desirable in the public interest, and who should operate and control various routes and services.

Regulation of radio differs from the Commission's control of common carrier service under Title II of the Act. 47 U.S.C. 201 *et seq.* Similar to agency regulation of common carrier transportation, the FCC fixes rates and decides the desirable extent of carrier competition. In contrast, the courts have repeatedly recognized that radio broadcasting, despite licensing, is an area of free competition. *Lorain Journal Co v. United States,* 342 U.S. 143 (1951); *Federal Communications Commission v. Sanders Brothers Radio Station,* 309 U.S. 470 (1940); *Easton Publishing Co. v. Federal Communications Commission,* 175 F. 2d 344, 346 (D.C. Cir., 1949).

In *Federal Communications Commission v. Sanders Brothers Radio Station,* 309 U.S. 470 (1940), the Court underscored the competitive nature of broadcasting:

> Thus the Act recognizes that the field of broadcasting is one of free competition. The sections dealing with broadcasting demonstrate that Congress has not, in its regulatory scheme, abandoned the principle of free competition, as it has done in the case of railroads, in respect of which regulation involves the suppression of wasteful practices due to competition, the regulation of rates and charges, and other measures which are unnecessary if free competition is to be permitted.

* * * * *

> . . . the Act does not essay to regulate the business of the licensee. The Commission is given no supervisory control of the programs, of business management or of policy. In short, the broadcasting field is open to anyone, provided there be an available frequency over which he can broadcast without interference to others, if he shows his competency, the adequacy of his equipment and financial ability to make good use of the assigned channel.
>
> * * * * *
>
> . . . Congress intended to leave competition in the business of broadcasting where it found it, to permit a licensee who was not interfering electrically with other broadcasters to survive or succumb according to his ability to make his programs attractive to the public. (Footnotes omitted) 309 U.S. at 474-475.

In *Carroll Broadcasting Co. v. Federal Communications Commission,* 258 F. 2d 440 (D.C. Cir., 1958), the court held that the doctrine of "free competition" was tempered only to the degree where it could be demonstrated, on the facts and after hearing, that such competition would result in harm to the public interest. But the court was careful to emphasize that the presumption is weighed heavily in favor of free competition and that the task of demonstrating injury to the public interest is "certainly a heavy burden." 258 F. 2d at 444.

The Commission's own rulings have held and reaffirmed the position that broadcasting is an area of free competition and that the FCC is powerless to consider the effects of the competitive impact occasioned by a new license. *Presque Isle*

Broadcasting Co., 8 F.C.C. 3, 9, 10 (1940). *Southeastern Enterprises (WCLE)*, 22 F.C.C. 605, 614 (1957):

> If the protestant's allegations are true and the public is injured in this case, it must persuade Congress to modify the law and provide for protection against competition in such cases as the protestant's. Until Congress gives us the power to permit something less than free competition in the industry, we have no power to save either the public or the protestant from certain of competition's uncomfortable effects.

The Congressional intent to preserve competition in the radio field was underscored by unsuccessful efforts to amend section 307(d) of the Communications Act in the 80th Congress. Section 307, 47 U.S.C. 307, requires the distribution of licenses among the several states to "provide a fair, efficient, and equitable distribution of radio service." The proposed amendment would have added "giving effect in each instance to the needs and requirements thereof." Hearings before the Subcommittee on Interstate and Foreign Commerce on S. 1333, 80th Cong., 1st Sess. (1947) demonstrated that the issue raised by the amendment was whether to remove broadcasting from the field of free competition, *Id.* at 40. The amendment failed.

In sum, the courts, the Commission, and the legislative history all uphold the principle that broadcasting is a field of free competition. The Commission's new CATV rules now limit this principle to free competition *among* broadcasters, but free *of* competition from any other medium. Such an overlacing is a corruption of the doctrine of free competition and entirely undermines the concept.

The Commission explains that CATV carriage of distant stations upsets regional exclusivity sales agreements between broadcasters and the networks. *First Report and Order,* 38 F.C.C. at 702, para. 50. The FCC's protection of these exclusivity agreements by restricting CATV competition is inconsistent with its finding in the *First Report and Order* that protection of copyright and copyright agreements are beyond the jurisdiction of the FCC. 39 F.C.C. at 740, para. 149. Additionally, it is inconsistent with the finding that the prohibition of rebroadcasting without permission under Section 325 of the Act, 47 U.S.C. 325, does not apply to CATV receipt and distribution of television signals. *Id.* at 704, para. 54, citing *CATV and TV Repeater Services,* 26 F.C.C. 403, 429-430 (1959).

The Commission's basic premise and rationale for CATV restrictive regulation is that CATV competition to broadcasters is "unfair." Despite the Commission's elaborate explanation of the economics of CATV operation and its advantageous competitive position, the Commission fails to explain under what precedent or rule of law such economic advantage takes on a tainted character of unfair competition. Nor does it explain why competition in itself has any unsavory or illegal aspects. The Commission is neither authorized nor competent to judge unfair competition. This function is designated to the Federal Trade Commission, 15 U.S.C. 45, which acts primarily to preserve competition – not to restrain it. To the extent that the Commission may consider antitrust violations or unfair trade practices in the grant or revocation of broadcast licenses,[34]

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[34] See *National Broadcasting Co. v. United States,* 319 U.S. 190, 223-224 (1943), holding that the Commission can consider and apply the antitrust laws in licensing.

it is bound by the FTC's standards and rules and the precedents of the courts. The FCC in launching a new regulatory scheme cannot create an independent body of law defining "unfair trade" practices.

In administering fair trade laws, the Federal Trade Commission refrains from regulating day-to-day business activity. It prosecutes and punishes offenders. In contrast, the FCC has constructed an entire system of economic regulation and seeks to impose daily operational rules and standards. Not only is the regulatory scheme unwise, but the premise of unfair competition is invalid. This Court held in *Cable Vision, Inc. v. KUTV, Inc.,* 335 F. 2d 348 (9th Cir., 1964), *cert. denied,* 379 U.S. 989 (1965), outside of possible copyright protection, broadcasters had no protectible interest against CATV competition.

Deference to the role of the FTC is made in Section 313 of the Communications Act, 47 U.S.C. 313, which directs the Commission upon a finding by the FTC to take certain punitive action against license holders. Findings of restraint of trade are left to the FTC, while the FCC acts upon this finding to withdraw the broadcast license.

The CATV rules are manifestly unreasonable and arbitrary where their foundation of unfair competition has no validity. They are likewise unreasonable and arbitrary when they relegate cable television to a role ancillary or supplemental to television broadcasting. It is certainly true that CATV in receiving broadcast signals off-the-air depends primarily upon broadcasting and in this sense supplements it. But the Commission has straight-jacketed CATV's future from its past. As a finding of scientific fact it is erroneous, since cable television (as the industry now prefers to be called) is fully capable of originating its own programs and sending

them independent of any broadcasting. As spectrum space is exhausted, cable television may open the door for unlimited, yet selective, television viewing.[35] Restricting and limiting its role to receive and distribute available television signals unfairly inhibits its growth to produce its own programs and materials, and denies the public of technological advance.

The regulations are also unreasonable and arbitrary in that they fail to achieve their announced purpose. The Commission explains that the CATV regulations are designed to promote local broadcasting, both existing and future. Additionally, the rules are to promote UHF development. First, that broadcasting is in need of any economic protection takes no small amount of tortured reasoning. The broadcast industry offers one of the largest returns on investment of any business in America.[36] It is the *only* "regulated" industry which under

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[35] In a recent article one of the Federal Communications Commissioners has pointed out that CATV has significant future potential to provide new communication services, such as printing of newspapers at home, shopping from home, and specialized teaching at home and by originating programming to meet special areas of interest. In this connection, he points out that CATV "might be a vigorous and useful check on the big telephone monopolies," but that it is unlikely that its future will "be as splendid as all this . . . Its fate is now being determined in a grim political and economic struggle with the giant interests whose prosperity and power it has challenged – the broadcast industry and the telephone companies." Nicholas Johnson, *CATV: Promise and Peril.* Saturday Review, November 11, 1967, p. 87.

[36] Figures released by the FCC in Public Notice 5317, dated August 25, 1967, entitled "TV Broadcast Financial Data – 1966," disclose that the broadcasters reported revenues of $2.2 billion with 87% of VHF stations showing profitable operations. Of these 116 stations reported profits in excess of $1 million.

these rules gets economic protection without any corresponding economic restraint — no ceiling or limitation is placed on its rates or return on investment. In contrast, common carrier by wire, in exchange for monopoly in routes, must charge just and reasonable rates as determined by the Commission. 47 U.S.C. 201(b).

Broadcast protection against competition is an unreasonable goal. The Commission began its regulation to preserve the spectrum space and distribute it fairly among responsible applicants. After a vested interest of broadcasters has developed, the Commission now deems its function has been enlarged to keep these interests free of competition and to force a new competitive industry and communications medium into an "ancillary," supporting service. Although the Commission's role is cast in the frame of "protecting the public interest," in practice it translates to "protecting broadcast interests" in maintaining an unchecked monopoly.

Secondly, the rules do not promote local broadcasting, and particularly, they do not promote UHF development. Their major thrust is in protection of the television stations in the 100 major markets, the healthiest and most economically rewarding stations. 47 C.F.R. 74.1107. The rules do little to aid local broadcasting since local broadcasting is not otherwise promoted by Commission practice and in practical effect does not exist. Approximately 90% of "local broadcasting" is made up of packaged network shows and national sporting events. The limping development of UHF is not due to CATV competition, but the Commission's own relegation of UHF to less desirable band frequencies and the Commission's failure to aid UHF stations in obtaining network affiliation. See

again the group that arrived first gets the Commission imprimatur and protection.[37]

In short, the CATV rules protect big television and the major networks, long recipient of Commission protection and free of Commission regulation. In practical effect, regardless of validity, the rules have bought time for the networks in the period where their private copyright litigation was winding its way through the courts.[38] If, of course, broadcast materials are subject to copyright then the Commission's major premise of unfair competitive advantage by CATV access to "free" materials is invalid, since private copyright will afford the necessary protection. On the other hand, if broadcasters are not entitled to private copyright protection, receipt and distribution of the broadcast materials cannot be labeled "unfair."

Administration of the CATV rules presents still another aspect of their tendency to unreasonable and arbitrary misapplication. The instant case is one in point. Here, petitioner has in its verified pleadings asserted that non-duplication will cause its demise. No contrary evidence – indeed, no contrary allegations – were made. The uncontroverted fact of the system's demise was ignored by the Commission in its opinion and order.

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[37] For a discussion of the failures of UHF development see Network Broadcasting, Report of the Committee on Interstate and Foreign Commerce, H. R. Rep. No. 1297, 85th Cong., 2d Sess. 226 (1958).

[38] The copyright case, *Fortnightly Corp. v. United Artists Television, Inc.*, 377 F. 2d 872 (2d Cir., 1967), *cert. granted*, 389 U.S. 969 (1967), is now pending before the Supreme Court, No. 618, and will be argued March 12, 1968.

In the *First Report and Order,* the Commission had concluded that non-duplication "need impose no substantial burden on the ordinary CATV operator or his subscribers," 38 F.C.C. at 714, para. 78, and where it did prove unduly burdensome, the Commission promised special action or waiver upon an appropriate showing. *Id.* at 715, para. 82. Here, the only statement pending before the Commission is that petitioner will be destroyed. This allegation is not challenged and the Commission makes no contrary finding. It simply ignored the fact. This practice is typical in the Commission's administration of its new rules. It is even more alarming in light of the fact the Commission did not inquire as to whether there was any corresponding harm on the part of the local stations necessitating destruction of the CATV system. Such callous administration of the rules is unreasonable and arbitrary.

In sum, the CATV non-duplication rules are an unreasonable and arbitrary restraint on legitimate CATV competition in that (1) they are inconsistent with the doctrine of free competition in the field of broadcasting as enunciated in the Act and its legislative history, the precedents of the courts, and the rulings of the Commission; (2) they are based upon erroneous premises of unfair competition and a supplemental role for CATV; (3) they fail to achieve their stated objective of protecting local and UHF broadcasting; (4) they are inconsistent with the findings that the Commission has no jurisdiction over copyright matters or rebroadcasting by CATV under Section 325 of the Act; (5) they impose unprecedented, economic regulation over non-licensees in favor of a vested class of licensees without any corresponding restraint; and (6) they are administered without due regard to the economic need and the corresponding economic damage in particular instances. Accordingly, the rules should be overturned.

B. Enforcement of the Non-Duplication Rules at the Option of the Local Broadcaster Is an Unreasonable and Arbitrary Restriction and Delegation of Authority.

Under the Commission's CATV rules, exclusivity is not automatic but must be invoked, oddly not by the Commission's action, but by action and request of the competitor television station under sections 21.712(g) and 74.1103(f). Section 74.1103(f) provides:

> Where a station is entitled to program exclusivity the CATV system shall, *upon the request of the station licensee or permittee,* refrain from duplicating any program broadcast by such station. [Emphasis added].

This rule places in the hands of the preferred TV broadcaster the power to invoke the rules at will. It delegates to the local station a degree of regulation and control over communications – matters which Congress has exclusively delegated to the Commission. The practical effect of this delegation of authority is to deliver CATV systems over to the hands of the local broadcasters. Where non-duplication protection threatens destruction of the CATV system, local broadcasters have life and death power over the system. Such economic leverage has naturally led to wide abuse. For example a station can extract a tribute from the CATV system in exchange for not invoking the rule. In other instances, the threat of invoking the non-duplication rules has kept a potential CATV system from starting its business. In one instance a local station "obtained" a minority stock interest in the CATV system in exchange for dismissing its objections to carriage of distant signals.

Astonishingly, the Commission approved this extortion. *United Transmission, Inc.*, 10 F.C.C. 2d 118 (1967). In other cases local television stations have conspired to gain the CATV franchise for themselves by manipulation of the non-duplication rule together with the threat of objection to new service by independent CATV operators. The CATV rules encourage restraint of trade and provide a means for gaining a monopoly in the same line of commerce.

If local carriage and non-duplication are desirable ends, and violations of these provisions are unfair, then they should be applied by the Commission fairly and evenly across the board. Discretion and control should not be placed in the hands of the competitor industry to administer at will or extract a penalty or tribute for not invoking them. This leverage in the hands of the preferred broadcaster does not achieve economic parity with CATV, but gives to the broadcaster the means for economic abuse and tyranny. Yet the Commission, cognizant of local deals and exchanges, encourages a local solution.[39] Manifestly, such an uneven administration of the rules at the whim of the competitor industry is an unreasonable and arbitrary delegation of authority leading to abuse and corruption of the rules themselves.

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[39] *First Report and Order*, 39 F.C.C. 683 at 737, para. 148 (1965).

CONCLUSION

For the foregoing reasons, petitioner prays that the Court enjoin, set aside, vacate and declare unlawful the order of the Federal Communications Commission as contained in its Memorandum Opinion and Order of November 17, 1967; that it declare unlawful the CATV rules promulgated by the Federal Communications Commission as beyond the jurisdiction of the Commission; that it declare unlawful the CATV non-duplication rules, 47 C.F.R. 21.712 and 74.1103, as a prior restraint in the receipt and distribution of information and an unreasonable and arbitrary regulation of a non-licensee industry; or in the alternative that it declare that petitioner is entitled to a full evidentiary hearing on its petition for waiver; and that it remand the matter to the Commission with instructions to conduct an evidentiary hearing consistent with the Court's opinion.

Respectfully submitted,

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March 8, 1968

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ Alan Raywid

...ited States Court of Appeals

FOR THE NINTH CIRCUIT

No. 22,393

GREAT FALLS COMMUNITY TV CABLE CO., INC.,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION
and
UNITED STATES OF AMERICA,

Respondents,

HARRISCOPE BROADCASTING CORPORATION,
SNYDER & ASSOCIATES,
TELEPROMPTER TRANSMISSION OF KANSAS, INC.,

Intervenors.

On Petition for Review of An Order of the
Federal Communications Commission

APPENDIX FOR PETITIONER

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APPENDIX A

Extracts of FCC Orders and Notices Regarding Regulation of CATV.[1]

I

Inquiry Into the Impact of Community Antenna Systems, TV Translators, TV "Satellite" Stations, and TV "Repeaters" on the Orderly Development of Television Broadcasting in Docket No. 12443, Adopted April 13, 1959, 26 FCC 403

IV. THE THREE BASIC LEGAL ISSUES

57. We have set forth for consideration herein three basic legal questions involved in any course of action we might adopt. These are: (1) what basis is there under present law, if any, for our assumption of licensing and regulatory powers over CATV systems (issue No. 11); (2) would it be legally valid for us to deny authorization for common carrier facilities for transmission of programs to CATV systems on the ground of adverse competitive impact on an existing local or nearby television station (issue No. 12); and (3) whether economic injury to a television station can be a valid public-interest justification for denial of authorizations to auxiliary services which compete with such station (issue No. 13). We consider these questions, in order, before proceeding to discuss the various proposed courses of action. 26 FCC 426

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[1] These extracts contain material repeatedly cited in Petitioner's Brief, principally from Commissioner Loevinger's dissents. It does not purport to present a complete or balanced statement of Commission policy or ruling on its regulation of CATV. Complete texts are available in the FCC reports.

Therefore, we adhere to our decision th
do not have jurisdiction over CATV's under section 3(h) and
II of the act, even though we assume (without deciding) they m
within the scope of section 3(a) which defines "wire communica
and includes "all instrumentalities, facilities, apparatus and
ices * * * incidental to such transmission." The other argu
advanced by Frontier in its petition for reconsideration (e.g., th
recognize economic impact upon broadcasting in our consider
of microwave common carrier applications) are considered else
herein.

62. *Jurisdiction over CATV's as "engaged in broadcastin*
Section 3(b) of the act defines "radio communication" as the "t
mission by radio of writing, signs * * * including all instrume
ities, facilities, apparatus, and services (among other things
receipt, forwarding and delivery of communications) incident
such transmission." Section 3(o) defines "broadcasting" as "th
semination of radio communications intended to be received b
public, directly or by the intermediary of relay stations." Se
3(cc) defines "broadcast station" as "a radio station equippe
engage in broadcasting as herein defined."

63. As for the suggestion that CATV systems are "instrume
ities" within the meaning of section 3(b) and that therefore (
they are engaged in the distribution of broadcast television prog
to these members of the public who reside in locations which
CATV can feasibly reach and who are willing to pay the ch

ed) they are engaged, in a sense, in "broadcasting," this would f itself give us jurisdiction to regulate these systems. Section the act provides in general that the operation of any apparatus e transmission of energy or communications or signals by radio be only pursuant to the act and in accordance with a license thereunder by the Commission. This section clearly does not e the transmission of programs by CATV systems, since such nission is by wire. We find no basis in the definitions contained ion 3 for the assumption of authority over these systems.

Regulation under "plenary power" over communications.—It is that we should regulate CATV's under our "plenary power" ommunications. Some parties have cited to us in this connecarious subparagraphs of section 303 of the act, under which we ipowered to classify stations, encourage the use of radio, make tions applicable to chain broadcasting, and generally make such ind regulations, not inconsistent with law, as may be necessary y out the act (subsecs. (a), (b), (f), (g), (i), (r)). However, not believe we have "plenary power" to regulate any and all rises which happen to be connected with one of the many aspects imunications.

Authority under section 325(a), or similar "property right" nt.—Section 325(a) of the act (which is in substance the same as rresponding section of the Radio Act of 1927) reads as follows:

> erson within the jurisdiction of the United States shall knowingly utter smit * * * any false or fraudulent signal of distress * * * nor shall any asting station rebroadcast the program or any part thereof of another asting station without the express authority of the originating station.

broadcasters argue that CATV systems are included within this ion, as "broadcasting stations" engaged in "rebroadcasting" actice, as already mentioned, it appears that CATV's seldom t to get such consent). They cite in support of this position ment by Senator Dill, one of the sponsors of the Radio Act of in connection with Senate consideration of that legislation. 8 Cong. Rec. 2880.) Therein, Senator Dill urged the adoption provision because otherwise a station would spend considerable for a program and it could then be picked up and broadcast other stations, "and particularly over the wired wireless, and charged for listening to it." The reference to "wired wireless" n as an indication that Congress had in mind wire retrans- n of the sort since developed by CATV systems. However, ion must also be given to the rest of Senator Dill's statement, reads as follows:

> The provision referred to does not prevent rebroadcasting, but it does r those who would rebroadcast to get permission from the original broad- r I do not think the construction placed upon the section by the gentle- ho sent the telegram is justified. Of course he cannot rebroadcast it, roadcasting is not publishing. It has a generally understood meaning, l *the reproduction by radio of the broadcasting waves.* [Emphasis il.]

ference to "reproduction by radio" in the last sentence would o exclude reproduction or distribution by wire as in the case of 'S.

66. We have in the past indicated our approach to a someh similar question, in our Report and Order on Amendment o R broadcasting Rules (1 R.R. (Pt. 3) 91: 1131). We were askl that proceeding to hold that section 325(a) was meant to prote t property right of whoever had such a right in the particular prog and that therefore consent should be required to be secured not n from the station rebroadcast but from the network station origin i the program, or the sponsor or advertising agency which bore the of producing it. We quoted Senator Dill's statement, and obs that it appeared that Congress intended to protect the property r in the program of those having such rights—in 1927 generall t station but now frequently others. We stated, however—

To the extent that section 325(a) may no longer accurately reflect p conditions or effectively carry out the original intent of Congress, the a ment of the section, or its repeal insofar as it pertains to rebroadcasts matter requiring legislative action.

67. We are of the same view today. It may well be that Con would desire to protect the property right of a broadcaster as ag CATV retransmission as well as against rebroadcasting. For reason, as well as because of the competitive impact involved we intend to recommend to Congress that an appropriate amend to section 325(a) be enacted, so as to extend the "consent" require to CATV's. But we do not believe that we can conclude that se 325(a) in its present form includes the requirement that CA get the consent of the stations whose signals they carry.

68. By other broadcasters, who do not urge that section 325(a) goes so far, we are asked to recognize the existence of a prop right, and to affirm it by rule; then, it is said, we would be in a posi to issue "cease and desist orders" against any CATV system rebr casting a signal without permission. This course of action we do believe appropriate. This is not the forum in which the existenc nonexistence of a private property right can be adjudicated; we in this connection that while CATV's have been in comme operation for nearly a decade, no serious prosecution of this c has yet been made by any broadcaster, as far as we are aware. U the existence of such a right is determined finally, either by jud decision or by congressional enactment, we cannot appropri consider a rule based on the assumption that it exists.

69. *Authority to regulate CATV's because of adverse effec broadcasting.*—It is urged by some broadcasters (often in conne with assertions made on the basis of secs. 3(b) and 3(o) menti above, or the "plenary power" theory) that we should regulate CA because they have a substantial adverse impact upon broadcas and tend to thwart what is our mandate under sections 1, 303, 307 to foster nationwide radio and television service, etc. Cited in connection are certain Supreme Court decisions dealing with the d industry (*United States* v. *Wrightwood Dairy Company*, 315 110 (1942), and *United States* v. *Rock Royal Co-op*, 307 U.S. 5 In the *Wrightwood* case the Court held that purely intrastate tribution of milk in competition with interstate commerce is sul to Federal regulation. Likewise, in *Houston, East & West T*

Railway Co. v. *United States*, 234 U.S. 342, the "*Shreveport* case," the Supreme Court held that the Interstate Commerce Commission could act to prevent a carrier from charging a discriminatorily low *intrastate* rate, though that Commission had no jurisdiction over intrastate rates as such. In short, it is argued, aside from the fact that CATV's are within some of the definitions of the Communications Act (although their being so makes the argument stronger), we can control them because of their effect upon broadcasting, clearly an interstate business and one which we are instructed to foster and lead to orderly maximum development.

70. Assuming this concept has legal validity (a point we believe is open to question, and upon which it is unnecessary for us to pass) in order to acquire jurisdiction on this basis, and *a fortiori* in order to utilize it, either in a rulemaking proceeding or on a case-to-case basis where we could consider whether or not a CATV system should be permitted entry into the field, we would have to make a finding that in a certain situation, or in situations falling within certain limits, there would be a substantial adverse impact on the local station. We have expressed above our inability to determine where the impact takes effect, although we recognize that it may well exist. Accordingly, we would find it impossible, from anything presented to us so far, to make the necessary finding, either in a particular situation or generally. Moreover, in any event, jurisdiction on this basis would exist, if at all, only in certain situations, and would therefore be a fractional approach to the problem. It is more appropriate to seek certain other specific remedies, discussed later herein. For these reasons we cannot appropriately proceed to regulate or control CATV's on this basis.

71. In sum, as to issue No. 11, we find no present basis for asserting jurisdiction or authority over CATV's, except as we already regulate them under part 15 of our rules with respect to their radiation of energy.

B. *The Economic Impact and Microwave Common Carrier Authorizations*

72. With respect to issue No. 12 in the notice of inquiry, it has been urged by most of the broadcasters that the Commission is obligated, in making the determinations of "public interest" under sections 307(a) and 309(a) of the Communications Act, to consider the impact upon a television broadcaster of the grant of radio facilities to a communication common carrier, where the common carrier facilities will be used for the purpose of providing communication service to a community antenna system operating in competition with the broadcaster. Implicit in this argument is recognition of the fact that it is not the common carrier which competes with the broadcaster or affects him adversely; it is the CATV. To embrace this argument would require the Commission to consider the content of the communications handled by the carrier, and the ultimate use to be made thereof.

73. In essence, the broadcasters' position shakes down to the fundamental proposition that they wish us to regulate in a manner favorable toward them vis-a-vis any nonbroadcast competitive enterprise. Thus,

for example, we might logically be requested to invoke a prohibit against access to common carrier facilities by such enterprises closed-circuit music and news services, closed-circuit theater televis operators, and, possibly, even ordinary motion picture and legitm stage operators, magazine and newspaper publishers, etc., compris all of the entities which compete with broadcasting for the time a attention of potential viewers and listeners. The logical absurdity such a position requires no elaboration.

74. We have heretofore partially answered this argument in opinion *In re Application of Intermountain Microwave*, 24 FCC 16 R.R. 733 (January 1958), which we now affirm. Enlarging up that decision, we now wish to make this point: the "public intere considerations which pertain to the grant of a communications co mon carrier application are not the same as, or interchangeable wi those which pertain to the grant of either a Broadcast Service ap cation or a Safety and Special Radio Services application. example, in the case of the latter, the Commission determines that public interest would be served by the allocation of certain frequenc for use by certain types of services. After this determination, all th remains, for each individual applicant, is to ascertain whether h legally, technically, financially, and otherwise qualified, and to der mine whether he falls within one of the stated eligible groups. In the case of a broadcast applicant, on the other hand, despite the exist ence of broadcast frequency allocations and service rules, a mo searching and complete "public interest" determination is made wit respect to each individual applicant, including an examination of the "content" of the service proposal. Thus, a broadcast applicant must not only show that he is legally, technically, financially, and otherwise qualified, but he must also show, for example, explicitly how his pro posed operations will serve the "public interest," including program plans and, under some circumstances, relationship to other medi of mass communications and other matters. In the case of the common carrier applicant, in addition to the showing of legal, technical, finan cial, and other qualifications, there is, typically, the necessity for show ing that there are no other public communication facilities availabl to do the specific job proposed; that the applicant is ready, able, and willing to serve all members of the public who may desire the service without discrimination; and that there is now in being one or more members of the public who require the service, or some reasonable expectancy that one or more such persons will present themselves if the facility is authorized.[26] There is no examination of the "content" of the intelligence which is to flow over the communication circu.

75. We are of the opinion that, in relation to the authorization of a common carrier facility, whether it be for a radio facility under title III of the act or a wire facility under title II, it is neither proper pertinent, nor necessary for us to consider the specific lawful use which the common carrier subscriber may make of the facilities of the carrier. To take a different view would place the Commission in the

[26] This simplified statement of matters to be considered is only an example. It seems obvious that competitive common carrier considerations, or other particular pro may involve other points of inquiry.

nomalous position of acting as a censor over public communications, nd put us under the burden of policing, not only the use of such acilities but the content of communications transmitted on the facilities. The logical extension of such a philosophy would require us o deny communications facilities of any kind (message telephone, elegraph, etc.) to CATV's and, for example, to deny access to faciliies to those acting contrary to our concept of the public welfare. The djudication of these matters is beyond our province.

76. Finally, we wish to emphasize that the rendition of common arrier communication service involves some situations which may be nique in the field of public utility regulation. The broadcasters hallenge the propriety of regarding specialized microwave relay facility operations, of the nature herein discussed, as being common carier operations. It is not unusual, in the communications field, to find carrier providing a regulated particular type of communication ervice over a particular route for a single customer. The carrier nay be one who offers a specialized type of service, as distinguished rom one who offers a general service. (See *In the Matter of Allocaion of Frequencies, etc., for a Theatre Television Service*, 9 R.R. 528, 1538–1539.) Also, it must be remembered that many comnunications common carriers traditionally and regularly provide ervices which are designated "private line services." Such services nay, for instance, comprise single or multiple communications paths o one or many points for a single customer. In a context more losely related to the instant problem, we point to the fact that many roadcasters utilize the services of Bell System Co., or independent elephone companies, where the carriers provide a tailor-made, espeially constructed microwave facility comprising an off-the-air pickup oint, and associated relays terminating in the broadcaster's studio. This is a typical broadcaster's private line common carrier facility vhere there is, in fact, only one user or subscriber involved and where nore than one such user on that particular facility is seldom, if ever, ontemplated or expected. On the contrary, many common carrier nstallations affording similar pickup and relay services for CATV ystems (as specialized carriers) provide such service to multiple subcribers simultaneously and operate with the continued hope and exectation that new and additional broadcast and CATV subscribers nay avail themselves of the use of the facility. In the communicaions field, these activities have always been treated and regulated as communications *common carrier* offering. We find no basis to warant a change in this regard at this time.

77. For these reasons, we conclude that issue No. 12 in this proeeding must be answered by a determination that it would *not* contitute a legally valid exercise of regulatory jurisdiction over common arriers to deny authorization for common carrier microwave, wire, r cable transmission of television programs to CATV systems on the round that such facilities would abet the creation of adverse cometitive impact by the CATV on the construction or successful operaion of local or nearby stations.

78. *Requiring that microwave communication common carriers how consent of the station whose signals they transmit.*—One of the

most common of the broadcasters' requests herein is that the micro-wave common carriers supplying the CATV's be required to show that they or their CATV customers have the consent of the station whose signal is picked up and transmitted for such use by the CATV. It is felt that while the direct requirement of CATV consent may be beyond the Commission's power at present, at least the Commission can impose such a requirement on its licensees, the microwave carriers who serve the CATV's. Some broadcasters put this in terms of character qualifications, arguing that relaying or transmitting without consent is "piracy," and that the Commission should not license facilities whose sole purpose is to engage in such activities, in line with its stated policy of considering violations of law on the part of an applicant in considering his application.

79. This contention is without merit. As we have noted, the matter of whether a property right exists has not been adjudicated, and we could therefore not appropriately impose this requirement upon the carrier, for the reason stated above in connection with the proposed rule requiring CATV's to have consent.

80. Accordingly, we are now considering a number of pending applications for microwave common carrier facilities on which we have withheld action during this proceeding, and we propose, as soon as practicable, to resume the normal processing of such applications.

C. *The Significance of Economic Injury*

81. Issue No. 13 herein calls for a determination as to whether economic injury to a regular television station can be a valid justification, in the public interest, for denial of authorization to an auxiliary service which would be in competition with the stations. The broadcasters say "yes," *when the economic injury affects the public interest*, as by causing the demise of the local station and resulting loss of a local outlet and, perhaps, the loss of the only service to outlying areas. Serious degradation of the station's service resulting from the impact is likewise urged as a public-interest consideration. NCTA and other pro-CATV parties urge that the Commission should take here the same position it has traditionally taken in economic injury cases—that as a matter of policy economic injury to an existing station should not be considered, both because it is impossible to predict the future in this respect (it is said to be even less susceptible of proof in the present context) and because the Commission has no public utility control over broadcasting operations, and cannot review their rates, costs, efficiency, and similar matters (*Voice of Cullman*, 6 R.R. 164 (1950); *Southeastern Enterprises*, 13 R.R. 139 (1957)). They urge that broadcasting is an *area of free competition*. On the other hand, the broadcasters refer to the fact that we took cognizance of the facts of competitive economic life in the UHF–VHF situation, ordering deintermixture in certain areas on that basis. They also assert that in effect we have already answered this question, in our rule making proceeding concerning translator authorization under this sort of circumstances (docket No. 12006). In disposing of that p

eding (Report and Order, FCC 57-886, 15 R.R. 1708 (1957)), we oted that the problem might well exist in some situations, but that so we could envisage situations in which the translator could operate the community (or a nearby community) without adversely affecting the regular station. We decided that the problem could better be handled on a case-to-case basis, in which we would consider e question in the light of such factors as terrain, the coverage of the anslator, the presence or absence of a CATV, the character of the egular" station (satellite, network, or nonnetwork, etc.)—factors hich should be thoroughly considered before determining whether translator should be disallowed. The broadcasters assert that therere we have already determined that economic injury is to be conlered, on an individual basis; they ask that we adhere to that posion. They say that they do not object to competition, or to our not king economic injury into account, where the question is one of *mpetition between regular broadcast stations*, between "likes," inead of the unequal, "unfair" competition which exists here between o different business activities which are not only on disparate comtitive footings but differ intrinsically in the extent to which they n serve the public interest.

82. In our recent holdings that we not only should not but legally uld not consider economic injury in the typical "new station in the arket" protest cases, we indicated a possible exception where 07(b) considerations" are involved (*Southeastern Enterprises, sua; West Georgia Broadcasting Company*, 14 R.R. 275 (1957)). In *rroll Broadcasting Company* v. *FCC*, 17 R.R. 2066 (July 1958), e U.S. Court of Appeals for the District of Columbia reversed our *est Georgia* decision, holding erroneous our view that the Communitions Act does not give us power to consider the effect of legal comtition. The court held that we must afford an existing licensee (in protest case) an opportunity to present proof of economic injury, nounting to public detriment, which would result from the grant of e application involved; if the evidence is substantial we must make dings on the subject.

83. Clearly, in the present series of situations there are "307(b)" nsiderations involved, since if the broadcasters' view is sustained, a mber of local stations may be forced off the air with resulting loss a local outlet and of the only service to some population. Therere, and considering the holding of the *Carroll* case, we believe our swer to the issue—as it is framed—must be "yes," as we intimated in r report and order referred to above. But we emphasize that in riving at this answer, all we say is that in authorizing a translator this kind of situation, or taking similar action with respect to other xiliary services, we will take into account—*when and to the extent at it can be established*—such adverse economic impact (of such aracter as to be of detriment to the public interest) as may result the local station. It should be noted, however, as the court pointed t in *Carroll*, that proof of such economic injury "is certainly a avy burden."

II

FIRST REPORT AND ORDER

(Microwave Relay to CATV) 38 FCC 683 (1965)

* * *

Opinion of Commissioner Loevinger Concurring in Part and Dissenting in Part in Dockets Nos. 14895, 15233, and 15971 (Proceedings re CATV's)

The Commission is issuing today a report and order, a notic inquiry and of proposed rulemaking, a memorandum on jurisdic and the text of new rules all of which relate to the problems pose community antenna television systems, commonly referred to

CATV's. These documents aggregate over 120 pages and set fo such a mass of detail that the outlines of the problem, as well as e basic issues, are somewhat obscured, if not wholly submerged. cordingly, it seems worth while to restate very briefly and simply w the problems and the issues are, in order to indicate my points agreement and disagreement with the majority.

A CATV is a system comprising an antenna for receiving televis signals, and cables and auxiliary apparatus (such as amplifiers) carrying the signals received into a number of receiving sets. CAT are about as old as commercial television itself, the first syste having been started as early as 1950. CATV's have been developed order to fill the wants of those who either because of distance terrain were unable to get television signals off the air in satisfacto quality or numbers. (See articles in Television Magazine, June 19, September 1964, and April 1965.)

For a variety of reasons, some of them related to actions of t FCC, the commercial CATV business has developed through in pendent companies which transmit or relay the signals and other co panies which distribute the signals to subscribers. Typically th will be an antenna on some high point near a community which ceives the signals of a number of TV stations. These signals will transmitted either by microwave relay or by coaxial cable to a poi in the settled part of the community. At this point the relay co pany will deliver the signals to the CATV operating company. T latter will maintain and operate the system which distributes t signals over wires to the homes of subscribers within the communit In some cases the relay company will deliver signals to several CAT companies.

CATV's were started in mountainous areas of Pennsylvania a Oregon where television reception was either poor or nonexistent f many communities. As it appeared that CATV's were able to bri good reception and offer a variety of services to communities f outside the major metropolitan centers, the companies spread to mo communities and got more subscribers. Over the years, as televisi has grown in both numbers of broadcasting stations and numbers homes, CATV has also grown, although by no means in proportio In rough figures there are now about 566 television stations in t United States covering some 266 markets (Television Magazine, Ap 1965, p. 85). Over 52 million U.S. households have television receiver which is 92 percent of all of the U.S. households, ibid. The CAT industry today has about 1,300 operating systems serving about 1 million homes (Seiden report to the FCC, p. 1). CATV's are co centrated largely in one- or two-station markets. Most systems a fairly small in size, about 90 percent having fewer than 3,000 su scribers and the average having about 655 subscribers. Most CATV deliver five signals to their subscribers, although some deliver as fe as three and some as many as seven or more, ibid. However, t number and size of CATV's is growing and CATV systems are bei offered to more communities, and to larger communities.

The proliferation of CATV's is regarded by many in the televisio business as an economic threat. It is said that while the broadcaste

as the burden and expense of providing programing which the audience gets without payment and which must be supported by advertising, the CATV operator simply delivers the broadcasters' programing to subscribers and receives payment from them. This is said to constitute unfair competition. It is also alleged that the competition is not only unfair but destructive in some situations, because CATV's deliver the signals of far-distant stations and deliver a relatively large number of signals to relatively small communities in which the audience is not large enough to support a number of stations. CATV's create the anomaly that some relatively small towns are provided with a greater choice of television programing over the local CATV than many larger cities have in the absence of CATV.

These circumstances have created a demand by many broadcasters for the FCC to take jurisdiction over CATV's and to institute measures to protect television broadcasters against competition of CATV's. As will be pointed out in some detail below, the FCC has instituted several proceedings and investigations relating to this matter. However, heretofore it has not taken any definitive action of general significance. While there has been some question as to the extent of the FCC jurisdiction, the Commission has had undisputed jurisdiction with respect to licensing microwave transmitting facilities for those relay companies that carry TV signals by microwave. The manner of exercising that jurisdiction is one of the matters that has been bitterly disputed and that is involved in the present proceedings.

By the documents which the Commission is now promulgating it adopts a series of measures which represent the conclusion of the Commission majority as to the action that the Commission should take in this field. There are four significant measures involved:

First, the Commission rules that CATV's must carry the signals of all local television stations without material degradation. The Commission exercises power over the CATV's by requiring licensed microwave relay companies to require their customers to comply with the Commission conditions.

Second, the Commission rules that the relay companies must require the CATV's which they serve to avoid the delivery to their customers of the television signals of any program which duplicates the program of any local station. This rule of nonduplication does not refer merely to simultaneous duplication, but requires CATV's to avoid presenting any duplicate program either 15 days before or 15 days after the date of broadcast by a local station. Thus, this rule provides that the CATV's served by the relay companies subject to the rule must avoid duplication of any local TV program for a period of 30 days.

Third, the Commission asserts jurisdiction over all CATV relay companies and systems, including those that are wholly intrastate and that transmit signals entirely by wire. Although this conclusion is called tentative, the background demonstrates that there is no practical possibility of dissuading the Commission from this conclusion. The Commission gives notice that the substantive measures already adopted will be extended to the full limits of this asserted jurisdiction as soon as the procedural amenities can be completed.

Fourth, the Commission institutes an "inquiry" seeking furth comment on more than a dozen and a half questions, all of th relating to the possibility of imposing further restrictions up the operations of CATV's.

It seems to me that in its approach to the CATV problem the Co mission is doing the wrong thing for the wrong reason in the wro manner to deal with the wrong problem. It is thereby erecting on a gossamer barrier against the evils which it fears.

The Commission is doing the wrong thing when it seeks to contr directly or indirectly, the specific programs which shall be present to the audience. The Commission is acting for the wrong reas because it seeks only to limit competition. The Commission is pr ceeding in the wrong manner because it is acting to extend its jur diction beyond statutory language and contrary to precedent. T Commission is dealing with the wrong problem because it concentrat attention only on the single matter of competition for listener attenti and substantially disregards more important and more basic problem Finally, the Commission is erecting only a gossamer barrier agair feared evils because the actions taken and proposed are not on wrong but must ultimately prove to be ineffective. Assuming that t Commission will assert jurisdiction over all CATV companies, a will impose nonduplication rules, and disregarding the risk that t action will be set aside for lack of jurisdiction, at best these ru will give slight and marginal protection against competition, and worst they will be wholly overturned on the whim of some futu Commissioner. This is not a sound basis on which to build an industr

Basically I concur in two of the four rulings made by the Co mission today and dissent from two of the four. I agree that t Commission should, within the scope of its jurisdiction, require CAT carriage of local television stations without degradation, and that should implement the rule so as to insure its effectiveness. I have disagreement with the substance of the rules regarding carriage local stations. I also agree that the Commission should undertake inquiry into the role and scope of CATV's, although I have some res vations as to the inquiry now initiated by the Commission. I disagr with the nonduplication rule which I believe is an improper attempt limit competition by controlling programing; and I disagree with t Commission's attempt to extend its jurisdiction without congressio authorization.

While I heartily agree that the Commission should conduct sweeping inquiry into the role and scope of CATV's in the field mass communications, it seems to me that the present inquiry is t little and too late. It is too little because it does not deal with fund mentals. Many of the important issues in the field are mentioned the notice of inquiry, but they are scattered through the somewh diffuse discussion in random fashion, even occurring in footnot But the basic issues are not mentioned. These are what the functi of CATV's should be, and what ultimate mode and system can developed or encouraged to provide the greatest service to the great number. In various paragraphs of the instant orders and opinio CATV's are discussed as being ancillary or subsidiary facilities

broadcasting and as being a service competitive with broadcasting. These concepts seem inconsistent to me, and differing regulatory consequences flow from them. For example, if the services are truly competitive, then there is some reason to prohibit or discourage joint ownership of broadcasting facilities and CATV's. On the other hand, if the services are ancillary, then that reason does not exist, and broadcasters should be permitted, and perhaps encouraged, to own CATV's. At the present time the Commission is deferring action on a large number of broadcast license renewals because the licensees also own CATV facilities. This action seems inconsistent with some of the positions adopted in these proceedings.

In any event, the present inquiry is too late because the Commission has already formed its opinion on this subject. I believe the Commission should make its investigation and conduct its inquiry before reaching its conclusions, rather than afterward. The documents issued today plainly show that the Commission and its staff have strong and fixed views regarding the subordinate place of CATV's in the mass communications system, and these views are not likely to be much influenced by anything that can be presented to the Commission in the course of the inquiry. Even if some Commissioners hold such views, it would seem to me to be more courteous, more productive and more wise to refrain from officially promulgating them until the formal "inquiry" has been completed.

In any event, I cannot agree that it is proper for the FCC to determine, either directly or indirectly, which programs shall be carried by a CATV system. It seems to me that the basic issue is whether the Commission should employ economic and engineering rules in order to achieve economic and engineering objectives, or should exert direct control over the substance of programing in an effort to achieve its objectives. The method of selective program control, which the majority adopts here, will beget future problems and more control. Problems will arise because of delay, changes in plans for broadcasting of particular programs, the requirements of section 315 and "fairness," and section 317, and other provisions, to pose only a few examples that can readily be foreseen of the numerous problems likely to arise under this rule. Suppose that a local station advises a CATV that the latter cannot carry some program because the station intends to carry it, and then the station, for whatever reason, does not carry the program? As a practical matter, the CATV will not have any other opportunity to carry the program once the date of its broadcast has passed. Will the FCC then require the local station to carry this program? Will that depend upon the Commission's determination of the value of the particular program? We know from experience that documentary and political programs are those most likely to be delayed or omitted. Will the Commission permit these programs to be taken off the CATV at the whim of the local station owner without insuring that he does carry them? It seems unlikely to me that the majority will be willing to do this. However, I doubt that those broadcasters who now clamor for a Commission rule on nonduplication will welcome this new grounds for Commission regulation of their programing.

Even more provocative questions are posed with respect to political programing. Suppose a distant station, carried on a local CATV, is carrying a series of political programs on a presidential election which is balanced as between the major parties. A local station decides to carry those network programs presenting the views of one of the two major parties. It notifies the CATV which then blanks out these programs on its circuits. The local station will then have to balance out its own programing by presenting the views of the other major party over its broadcasting facilities. But the programs of the distant station carried on the local CATV will be unbalanced since they will present only the programs presenting the views of one party. Most important, the local public will then have an unbalanced presentation since it will have the programs favoring one party presented over two stations on the local system, whereas the programs favoring the other party will be presented over only one of the local channels and there will be only half as many of the latter. This is obviously a device that could easily be used to give the public a very biased political presentation during a campaign. Is the FCC then going to supervise CATV systems to see that their programs comply with all of the requirements of section 315 and "fairness"? How will this be accomplished? Will the FCC require program origination by CATV's? These and a host of other problems flow directly and inevitably from the approach adopted here. To say that any single situation is unlikely is not an adequate response. The records of the FCC and its own attempts to influence programing are eloquent testimony that situations such as those suggested, and others more bizarre and unusual, do occur and recur.

It should be noted that the rules now adopted by the Commission are based, in significant part, upon its concern for the preservation of "local live" programing, and that the notice of inquiry suggests that the protection which the Commission is now bestowing upon broadcasting stations is likely to be "accompanied by a concomitant duty on the part of the station" to provide "local live" programing. (See notice of inquiry, par. 53.) Thus, the nonduplication rule is not only a direct intrusion into the programing area through control of CATV's, but is also another argument to buttress the case for further Commission control of the programing of broadcasters. Believing as I do, that the Commission should not seek to control program content in the field of broadcasting, I am opposed to this approach. See separate opinions in *Lee Roy McCourry*, 2 R.R. 2d 895 (1964); *George E. Borst et al.*, FCC 65–207 (1965); The Role of Law in Broadcasting 7 J. of Bdcsting. 113 (1964); Religious Liberty and Broadcasting, 3[illegible] Geo. Wash. L.R. (March 1965).

One practical factor that seems to be left out of consideration in the adoption of a nonduplication rule is that this is the approach which i[s] most likely to provide incentive, if not virtual necessity, for CATV' to undertake the origination of their own programs. The operatio[n] of the nonduplication rule means that the CATV operators are re[-] quired to delete material from the programs which they receive an[d] deliver to subscribers and it also means that when such material [is] deleted the CATV is left with a vacant channel. While the economi[c]

pressures and motivations will undoubtedly vary from situation to situation, this kind of situation provides both the opportunity and incentive for program origination; and therefore, in the long run, is likely to engender more competition for the local television stations than it avoids. It seems to me to be far more simple and effective, not to mention wise and appropriate, to require that CATV's shall carry local stations, that they shall not alter or degrade the signals that they carry and that they shall meet such other engineering requirements as may be found appropriate, and to leave determination of programing to the broadcasters without forcing the CATV operators into the area of program selection and encouraging them to enter the area of program origination.

The most important and fundamental legal objection to the present Commission action is its lack of adequate jurisdictional basis. The rule promulgated by the Commission at this time undertakes to regulate the programs that may be carried by CATV's by requiring common carriers that serve the CATV's to impose upon their customers, as a condition of service, the limitations contained in the Commission rules. The Commission has repeatedly rejected this basis of jurisdiction in the past, as appears from the cases cited and quoted below. But regardless of lack of support in precedent or statutory language, the logical implications of this approach should warn of its unsoundness. If the Commission can impose its will on a person or business entity, that is the customer of a common carrier, by the simple device of requiring the common carrier to act as the Commission's policeman in order to keep its license, then the Commission can regulate any business in the United States. Every business and most citizens are customers of the telephone and telegraph companies. It has never previously been suggested that this fact subjected them to regulation by the FCC. But if today's decision stands, then that is the law. The Commission need no longer be constrained by any technical limitations on its jurisdiction arising from statutes enacted by Congress, if this theory is sustained by the courts. The rule adopted by the Commission today applies to CATV's served by the telephone company as well as to those served by CATV relay companies. But there is nothing in the logic of the Commission's jurisdictional approach that limits this technique to CATV's. If this jurisdictional foundation is sound for CATV's, the Commission may, by precisely the same technique, impose its regulations on theaters or newspapers, on stockbrokers or taxicabs, indeed on any business or person that needs and uses the services of a communications common carrier.

The Commission's assertion of direct jurisdiction over companies that receive broadcast signals and transmit them wholly by wire within a single State, without any specific statutory foundation, is equally alarming in its implications. The principal argument urged in support of the Commission's jurisdiction over such companies is that it is desirable for the FCC to have such jurisdiction in order to attain the broad general objectives of the Communications Act. However, if this reasoning is sound, then the jurisdiction of the Commission is literally unlimited. There is scarcely any aspect of organized social living that is not in some way related to the complex ramifications of

the communications system that is now under the jurisdiction of t Commission. If the Commission has authority to deal with any a tivities which "threaten to impede realization of the Commissio * * * plan and policies" (memorandum on jurisdiction) then it c control all amusements, the field of journalism, the scheduling of mov ments by trains, planes, and ships, not to mention almost any oth activity that is either competitive or ancillary to or an important us of communications. Such vague and broad reasoning simply will n sustain jurisdiction as to activities not plainly within the scope of so more specific statutory language. See *F.P.C.* v. *Panhandle Co.*, 3 U.S. 498 (1949).

When the Communications Act itself is examined it is found th not only is language lacking to give the Commission jurisdiction whi it undertakes to assert here but the language of the statute express denies that jurisdiction.

Section 1 of the act, 47 U.S.C. 151, states the purpose of the act most general terms and states that the FCC is created pursuant this purpose. However, it does not define or confer any jurisdictio

Section 2 of the act, 47 U.S.C. 152, says in its first subdivision th "the provisions of this chapter shall apply to all interstate and forei communication by wire or radio * * *." It does not state that t Commission has jurisdiction over all such communication. Rather describes in general terms the scope of the act and the outermost lim tations of its application. However, it says that within these out most limits the act applies pursuant to its provisions. In other wor in order to find jurisdiction within the scope described by the fi subdivision of section 2, it is necessary to find some specific provisi of the act conferring jurisdiction.

This is emphasized by the second subdivision of section 2, whi specifically says that nothing in the act shall be construed to give t Commission jurisdiction with respect to "intrastate communicati service by wire or radio of any carrier" or "any carrier engaged interstate or foreign communication solely through connection radio, * * * with facilities located in an adjoining State * * * another carrier * * *." It would seem that the latter clauses speci cally exclude both CATV relay companies and CATV's from t jurisdiction of the Commission when they do not use microwa However, it is argued that the intrastate relay companies using wi rather than microwave, are connected by radio with *broadcasters* another State rather than with *carriers* in another State. The obvio answer is that at the time of enactment of the Communications A such things as CATV's were unheard of and that the intent of Congr expressed in the second subdivision of section 2 is to deny the Comm sion jurisdiction over intrastate carriers which are not part of a sing integrated system and which simply carry signals emanating fr another State. The congressional intent to exclude the Commissi from regulation of intrastate facilities and operations is indicated a number of provisions in the Communications Act. In addition the restrictions of 47 U.S.C. 152(2), a statutory denial of Commissi jurisdiction to regulate intrastate facilities or operations appears 47 U.S.C. 214 as to communications common carriers, in 47 U.S.

221(b) as to telephone companies, and even in 47 U.S.C. 301(d) as to radio signals which do not have a direct effect on interstate communications.

However, it is not necessary to rely upon inferential construction. Examination of the entire Communications Act for a specific provision applicable to companies engaged in transmitting signals intrastate by wire discloses that only section 214, 47 U.S.C. 214, is applicable. This section provides that no carrier shall construct or operate a line without obtaining authority from the Commission provided, however, that no authority from the Commission is required for the construction or operation of "a line within a single State unless such line constitutes part of an interstate line." The section further provides that, "As used in this section the term 'line' means any channel of communication established by the use of appropriate equipment other than a channel of communication established by the interconnection of two or more existing channels * * *." Thus, by specific statutory provision, the mere fact that a CATV system or relay company is connected by radio to some other communications facility does not constitute its lines a part of a channel of communication comprising both the out-of-State facility and the intrastate facility. The company which operates by wire within a single State is, therefore, specifically excluded from Commission jurisdiction by section 214. By familiar rules of statutory construction such a specific and explicit exclusion prevails over any inference that might otherwise be spun out of more general language that is claimed to imply jurisdiction.

The Commission memorandum on jurisdiction argues from the definitions of "wire communication" and "radio communication" in 47 U.S.C. 153, to the conclusion that the Commission has jurisdiction over CATV's because their activities may be said to come within the scope of these definitions. This argument is wholly beside the point. The section on definitions confers no jurisdiction at all. Many terms are defined in that same section, including the terms "United States," "person" and "State commission." It is obvious that the FCC does not have jurisdiction over the United States, over State commissions or over all persons. The terms defined have legal significance only to the extent that they are used in other sections of the statutes. But one will search the act in vain for any section which expressly confers jurisdiction upon the Commission in the broad terms mentioned in the memorandum on jurisdiction. Consequently, the definitions given those terms are not germane to the issue.

If the argument in the Commission's memorandum is correct, then the Commission has jurisdiction not only over intrastate wire relay systems and CATV operating systems but also over television and radio receivers. The argument made in the Commission memorandum is that any instrumentality which is incidental to or used in the process of transmitting picture or sound or which forms a connecting link in the chain of communication between the transmitting station and the viewing public is subject to Commission jurisdiction. Television and radio receiving sets are just as much within this jurisdictional concept as CATV's and broadcasting stations. In that event the "all channel law" (Public Law 87–529, 47 U.S.C. 303(s)) was unnecessary as the

Commission had full authority to regulate and license receivers by th terms of the original Communications Act. Clearly, neither the Com mission nor the courts have ever previously thought this to be the case Both have continuously acted on the contrary assumption.

The Commission itself has explicitly denied its right to control an its jurisdiction over CATV's in several decisions which up to th present time have not been specifically reconsidered or overruled The first reported decision is *Intermountain Microwave*, 24 FCC 54 adopted January 30, 1958. In this case, a television broadcaster. Hi County, objected to the grant of a microwave authority to a CATV relay company. The Commission opinion said:

> Hill County is seeking to have the Commission deny a radio authoriza tion to a communications common carrier because the communication circu to be derived under such authorization will be utilized by subscribers wh are competitors of Hill County in endeavoring to provide visual entertain ment * * *. We are of the opinion that the request of Hill County mus be denied. * * * In considering this problem, it must be remembered tha it is possible and feasible for communications common carriers to provid program relay facilities to subscribers where no special authorization i required from this Commission. e.g., where the carrier already has i place properly authorized general cable, wire, or radio facilities which ma be put to such particular use in the ordinary course of business. Thu to single out for special consideration and denial only those situations wher new construction is involved, where such new construction is specifically fo the purpose of providing a service to the public, when the initial or sole use availing himself of service is a community television distribution system would be arbitrary, capricious, and discriminatory. An alternative, c course, would be to adopt an overall policy, rule, or condition with respe to every cable, wire, or radio authorization, issued by this Commission t carriers under its jurisdiction, under both title II and title III of the Com munications Act, prohibiting the rendition of the specific type of servic here under attack by the objectors. Such a procedure would be equall arbitrary, capricious, and discriminatory and unwarranted in view of ou ultimate determination herein.

A few months later, in *Frontier Broadcasting Co.*, 24 FCC 25 16 R.R. 1005 (1958) the Commission specifically pointed out that eve if it held CATV systems to be common carriers they would come wit in the scope of section 214 of the Communications Act and, therefor would not require Commission authority to construct or operate intr state lines. The Commission further said that when CATV system transmitting signals by wire do not emit excessive radiation they i volve no radio transmission which requires any form of license fro the Commission under the act.

Thereafter the Commission conducted an extensive inquiry an after plenary proceedings entered a report and order considering t whole subject of CATV and repeater service, 26 FCC 403, 18 R.R. 15 (1959). The following are some of the conclusions then reached a stated by the Commission:

> * * * we find no present basis for asserting jurisdiction or authori over CATV's except as we already regulate them under part 15 of our ru with respect to their radiation of energy. (Par. 71.)
>
> * * * it would *not* constitute a legally valid exercise of regulato jurisdiction over common carriers to deny authorization for common carri microwave, wire, or cable transmission of television programs to CA systems on the ground that such facilities would abet the creation adverse competitive impact by the CATV on the construction or successf operation of local or nearby stations. (Par. 77.)

> Certainly, with respect to anything more than the barring of simultaneous duplication, we believe this to be an unwarranted invasion of viewers' rights to get "live" programing if they are willing to pay for it. The suggested rules restricting presentation of the programs of the local station's network would appear to be cumbersome, if not completely unworkable, especially considering that many stations in small markets, including some of those covered in the record, present programs of two or even three networks. (Par. 96.)
>
> We have considered herein the problem, the issues raised, and suggested methods of solution. Two of the broadcasters' suggestions, both relating to CATV's, we adopt. These are that CATV systems should be required to obtain the consent of the stations whose signals they transmit and that they should be required to carry the signal of the local station (without degrading it) if the local station so requests. *Since both of these steps require changes in the Communications Act*, we will shortly recommend to Congress appropriate legislation, as indicated above. (Par. 99; emphasis added.)

In 1962 the Commission, with one dissent and one abstention, issued the *Carter Mountain* decision, which is the principal reliance of those who now argue for FCC jurisdiction in this matter. *Carter Mountain Transmission Corp.*, 32 FCC 459 (1962). In this case a CATV relay company applied for authority to transmit television signals by microwave to a small community with one local television station. The television station protested the application and a hearing was held. On the basis of a complete evidentiary record the Commission found that a grant of the microwave authority to the relay company with the bringing of CATV service to the community would result in the demise of the local television station. It, therefore, found that a grant of the microwave authority would not be in the public interest. The Commission stated that the two basic issues in the case were whether the relay company was a bona fide common carrier and whether the economic impact of the grant was of legal significance or the public interest was inherent in the fact that applicant was a common carrier. The Commission held that economic impact of the proposed grant on the broadcasting station was of legal significance and was adequate ground for denying the authority sought. The holding was explicitly limited to this. The Commission said in its opinion: "There is no attempt to examine, limit, or interfere with the actual material to be transmitted. We are merely considering the question of whether the use of the facility is in the public interest, a conclusion which must be reached prior to the issuance of the grant." The Commission did not consider or discuss the decisions cited above and the only comment in *Carter Mountain* on the earlier decisions is this: "To the extent that this decision departs from our views in the report and order in docket No. 12443, 26 FCC 403 (released April 14, 1959), those views are modified."

The decision was appealed and affirmed by the court of appeals. In the court of appeals, six issues were agreed upon between the parties and submitted to the court by stipulation. These are set forth in the appellate opinion. *Carter Mountain Transmission Corp.* v. *FCC*, 321 F. 2d 359 (C.A.D.C. 1963), cert. den. 375 U.S. 951 (1963). None of the issues related either to the imposition of conditions upon or control over the programs to be carried by the applicant or to the possibility of extending FCC jurisdiction to companies not utilizing radio trans-

mission for the carriage of signals. In fact, the Commission in its brief to the Supreme Court in opposition to certiorari, specifically stated that no question of Commission jurisdiction over CATV's operating by wire was involved in that case. The brief stated "* * * several bills have been introduced in Congress to give the Commission direct authority over CATV's, *a question not involved here*, * * *" (FCC brief, p. 10; emphasis added).

A month after issuing its *Carter Mountain* decision, the Commission issued a unanimous order in *WSTV, Inc.* v. *Fortnightly Corp.*, 23 R.R. 184 (1962) in which it relied upon and reaffirmed the holding of the *Frontier Broadcasting* decision, and reiterated that "this Commission [is] without title II jurisdiction over the CATV systems." Accordingly, the Commission ordered that the complaint by a broadcaster against a CATV system "is dismissed for failure to state a cause of action within the jurisdiction of the Commission."

In the report and order adopting rules to be imposed on CATV's through the common carriers which serve them, the Commission merely mentions the matter of jurisdiction in a footnote (footnote 5). This cavalier reference relies entirely on the authority of the *Carter Mountain* case as the legal foundation for jurisdiction to issue the rules. But this reliance is wholly misplaced. The *Carter Mountain* decision held only that the Commission could wholly deny a common carrier application when the sole proposed use of the common carrier was to serve a CATV and such service would, on the facts of record in that case, result in the economic destruction of a local broadcasting station. The issue of Commission authority to impose conditions on or control the character of the signals carried by the relay company, not to mention the customer, was not raised or decided in that case, was not considered by the Commission (see par. 3, 32 FCC 460) and, in fact, was expressly disclaimed by the Commission (par. 8, 32 FCC 462). The Commission did say that its denial of the application was without prejudice to the right of applicant to file a new application when conditions had changed so that the operation of the CATV would not have the impact on the local television station which the record there demonstrated was likely to follow in circumstances prevailing at the time of the decision. However, this is a far cry from a holding that the Commission can impose conditions as to the signals to be carried by the communications carrier or by its customer. As noted in the preceding discussion, the Commission told the Supreme Court in the *Carter Mountain* brief that the issue of FCC jurisdiction over CATV's was *not* involved, and shortly after the *Carter Mountain* decision a unanimous Commission reaffirmed that it did *not* have jurisdiction over the carriage of signals by CATV's. There is no reasoned Commission opinion that considers this issue and concludes that the Commission does have the jurisdiction actually exercised in the instant report and order. Several Commission opinions hold to the contrary. In these circumstances, the casual disposition of the jurisdictional issue in a footnote seems inadequate at best and irresponsible at worst.

The Commission memorandum cites cases like *American Trucking Assn.* v. *U.S.*, 344 U.S. 298, and *NBC* v. *U.S.*, 319 U.S. 190, to sustai

jurisdiction. However, the point at issue in those cases, and others like them, was simply whether a regulatory agency having jurisdiction over a field of activity and an enterprise within that field could act with reference to a particular practice not specified in the basic statute. The Supreme Court held that, regardless of the absence of specific reference to a particular practice in the act, the regulatory agency having jurisdiction of the field and the enterprise might promulgate regulations dealing with a practice which was considered to be an evil requiring correction. The Court points out that the necessity of formulating regulations to meet specific practices not foreseen by Congress is precisely one of the reasons regulatory agencies such as the Commission are created. However, this reasoning has nothing whatever to do with an issue as to the existence of jurisdiction over an economic or technical field or a particular enterprise.

A case much closer to the present situation than any cited in the Commission's memorandum is *F.P.C.* v. *Panhandle Co.*, 337 U.S. 498 (1949). In that case the Supreme Court held that the FPC could not extend its power by the kind of reasoning relied on by the FCC here, even though the FPC was seeking to regulate a company concededly within its general jurisdiction but as to an aspect of the company's business that was not within the terms of the statutory jurisdiction. The Court said, inter alia:

> Nothing in the sections indicates that the power given to the Commission over natural-gas companies by section 1(b) could have been intended to swallow all the exceptions of the same section and thus extend the power of the Commission to the constitutional limit of congressional authority over commerce.
>
> Failure to use such an important power for so long a time indicates to us that the Commission did not believe the power existed. In the light of that history we should not by an extravagant, even if abstractly possible, mode of interpretation push powers granted over transportation and rates so as to include production * * *. We cannot attribute to Congress the intent to grant such far-reaching powers as implied in the act when that body has endeavored to be precise and explicit in defining the limits to the exercise of Federal power.

The Court stated that if the Commission were of the opinion that it should have the power sought, then it was authorized to call the attention of Congress to that fact. The reasoning adopted by the Court in the *Panhandle* case applies with even greater force to the FCC in the instant situation. Here there is not merely an inference from earlier inaction that the Commission did not believe it had the power now asserted. Here there are clear and explicit declarations by this Commission that it does not have the power which the present majority of the Commission now claims. The only thing that has changed since the Commission last disclaimed the jurisdiction it now asserts is the personnel of the Commission. That is not a proper basis for disregarding precedent and changing established legal principles. See my separate opinion in *Assignment of Additional VHF Channel to Johnstown, Pa., etc.*, 1 R.R. 2d 1572, 1580 (1963).

Contrary to the apparent belief of the Commission majority, the fact that it might be thought desirable for the FCC to have control

of CATV's or their practices does not indicate that the agency does possess such power. See *Youngstown Co.* v. *Sawyer*, 343 U.S. 579 (1952). Despite some reservations as to the wisdom and objectivity of the Commission and its staff regarding CATV's, I would agree that, as a matter of principle, the FCC should have the authority to regulate CATV's as a service closely related to broadcasting. I favor and will support appropriate congressional legislation to give the Commission jurisdiction in this field.

This position differs from the assertion of jurisdiction made by the Commission in the instant proceedings in several important respects. First, it is founded on a deferential respect for the constitutional scheme by which Congress must specifically delegate power before it is exercised by an agency created by Congress. Second, the power that Congress delegates is almost certainly going to be specified and limited in extent, whereas the power derived by inference from broad general statutory terms is unlimited except by the self-restraint of the Commissioners and the vigilance of the courts. Finally, it is likely that congressional hearings will illuminate this problem and that Congress will provide some guidance to the Commission that may suggest a better course that the one the Commission is now determined to follow.

At least part of the problem that the Commission now foresees in the proliferations of CATV's is the result of the Commission's own past policies. In the past the Commission has adopted the same restrictive attitude toward translators and other auxiliary services that were within its jurisdiction that it now proposes to take toward CATV's. The popular demand which has been responsible for the recent rapid growth of CATV's has been largely the result of the denial of service to many areas because of the FCC strictness and reluctance in granting authority for the construction and operation of translators and boosters. Apparently the Commission has not yet learned that the expansion of service is not to be attained by the limitation of competition and the imposition of rigorous regulation but rather by stimulating competition and moderating regulation. The Commission can do many things to stimulate and encourage the extension and expansion of television service throughout the country, but regulating the programs that can be brought into homes by CATV's and extending the Commission's jurisdiction without specific congressional authority are not likely to help.

However, it seems to me that the most basic and important issue involved here is far more important than the interests of the broadcasters, the CATV's, or even of the audience in securing broadcasting service. The basic issue involved here is whether a great Government agency will show reasonable respect for its own precedents and reasonable restraint in seeking to extend the scope of its own power. Undoubtedly the independent regulatory agencies have been given great power and broad discretion in its exercise. But if democratic government is to survive, the corollary of great power and broad discretion must be a strong impulse of self-restraint in the exercise of such power. In the face of statutory language, the Commission's own precedents

the prior statements of the Commission to the courts and its requests to Congress for legislation on this subject, it seems to me to be presumptuous for the Commission now to assert jurisdiction which it has previously explicitly disclaimed. If the laws are inadequate to cope with the problems of the moment, it is the function of Congress to remedy that lack. There is no reason to assume that Congress is any less responsive than the Commission to the public interest, or that it is unable or unwilling to act if action is needed in this field at this time. I am, accordingly, compelled to dissent from the Commission's efforts to extend its jurisdiction without specific congressional authority.

III

SECOND REPORT AND ORDER

* * *

Separate Statement of Commissioner Lee Loevinger Re Second Report and Order in CATV Proceedings

I concur in the substantive provisions of the order but I cann join in the opinion or agree that the Commission has the jurisdictic which it now asserts.

The opinion (here called "second report") which purports to su port the present order seems to me to illustrate many of the wor aspects of the institutional decision. The opinion does not reall rationalize or justify the result reached, but rather accepts it som what grudgingly. This is a product of the fact that the opinion wa originally drafted by the staff to support an entirely different result Despite the efforts and instructions of the Commission, and a serie of revised drafts, the instant opinion is substantially similar to th document which was written to support a different result. The opin ion refers to little evidence and much of that is inconsistent, assump tions and speculation substitute for facts, the reasoning is circuitou and illogical, and the statement is so turgid and prolix that it doe more to obscure than illuminate the subject. I can concur fully onl in paragraphs 97, 98, 150, and 156 to the extent of my concurrence i the order.

What the Commission is doing in the instant order is to exercis its quasi-legislative powers. Consequently the decision to issue o join in the instant order is a legislative judgment. I concur in th substantive provisions of the order not because I think it is wholl logical or the best method of dealing with the subject, but because i seems to me to be the best and most reasonable proposal that has an practical chance of securing approval by a majority of the Commis sion. This is, in my opinion, a legitimate basis for making a legisla tive judgment.

On the other hand, the assertion of jurisdiction is a legal matte that requires a legal judgment. Nothing has appeared or occurre since the previous Commission statement on this subject that furnishe any basis for reaching a different conclusion as to jurisdiction tha the one set forth in my prior opinion. (38 FCC 683, 746 (1965). Accordingly I adhere to that opinion and to the conclusions state there.

The Commission rule requiring a hearing before CATV is permitte to commence operation in any of the 100 largest markets is particularl questionable. The ostensible justification is that CATV might be come pay-TV. This reason is flimsy, since that danger—if it is danger—could be met much more easily by less burdensom requirements.

Nevertheless the substantive position now adopted by a majority o the Commission seems to me to be the most moderate and reasonabl compromise of sharply conflicting views and positions that has an practical chance of approval. It is of the greatest importance tha the Commission now recognizes the necessity of requesting Congres to legislate on jurisdiction and other important aspects of this matte and has done so. In these circumstances, I think the most construc tive and useful course is to support affirmative action by the Commi sion, leaving the jurisdictional issue to decision by Congress and th courts, and looking to Congress for further guidance as to regulator matters. Accordingly I concur in the substantive provisions of th legislative rules now promulgated by the Commission.

IV

MEMORANDUM OPINION AND ORDER IN DOCKET NOS. 14895 AND 15233 AND 15971, ADOPTED MAY 25, 1966

(On Petition for Reconsideration of Second Report and Order)

Dissenting Statement of Commissioner Robert T. Bartley

I dissent. I would grant the petitioners' requests to stay the effectiveness of the Commission's CATV rules pending action on their petitions for reconsideration, until final adjudication of appeals from the second report and order, or action by Congress, whichever should occur first.

I disagree with the Commission's finding that there is little likelihood of petitioners' prevailing.

There are presently six bills pending in Congress with respect to regulation of CATV, H.R. 7715, H.R. 12914, H.R. 13286. H.R. 14201, H.R. 14454, and S. 3017. Hearings have been held on four of these

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bills by the House Interstate and Foreign Commerce Committee (H.R. 7715. H.R. 12914, H.R. 13286. and H.R. 14201).

I believe it is unsound to second-guess the Congress, and now conclude that no changes will be made in the Commission's proposed bill. H.R. 13286. With substantive changes or enactment of a different bill, the Commission's present CATV rules could be nullified.

Moreover, in face of serious questions as to the Commission's having jurisdiction over CATV and validity of the rules recently promulgated, there is no certainty that the rules will be upheld in pending court appeals.

In my opinion, the Commission does not presently have jurisdiction over CATV and, consequently, the rules are invalid for this and other reasons set forth in my dissent to the Commission's decision in docket No. 16551, which dissent is incorporated herein by reference and attached hereto.

I vote to stay the effective date of the rules until their validity has been finally adjudicated by the courts or until Congress has enacted CATV legislation. 3 FCC 2d 827-828

Dissenting Statement of Commissioner Robert T. Bartley

I dissent. In the absence of congressional action, I agree with the respondent's contention that the Commission does not have jurisdiction over CATV systems and that, consequently, the rules adopted in the second report and order are invalid. Even assuming, arguendo, that the Commission does have jurisdiction, I believe that section 74.1107 of the rules is invalid because it contravenes section 4(c) of the Administrative Procedure Act, which provides that a substantive rule not be made effective in less than 30 days after required publication "except as otherwise provided by the agency upon good cause found and published with the rule."

Section 74.1107 was made effective immediately upon the required publication. A recitation of good cause found was made on the basis of injury to the public from continued implementation of service extending grade B signals.

In my opinion, injury to the public was not supported with any factual indication or showing and was purely unfounded speculation. There appeared to be more indication of benefit, rather than injury, to the public from the extended service in question. Consequently, the recitation of good cause found was, I believe, a nullity under section 4(c) of the Administrative Procedure Act, and the immediate effective date of the rule rendered it invalid.

The February 15 cutoff date of section 74.1107(d) appears in practical operation to be a retrospectively applied effective date of the rule itself and, accordingly, a further ground for invalidity of the rule.

Moreover, I believe that section 74.1107 is not valid because adequate notice was not given on the substantive provisions imposed on implementation of service in the top 100 markets. Also, the mandatory hearing requirement seems extremely arbitrary and excessively burdensome on a CATV applicant. A serious question exists as to what kind of possible showing a CATV applicant could make to prevail against the fears expressed by the majority in the second repor and order.

A basic fallacy of the CATV rules is the rationale which the Com mission used to justify its assertion of jurisdiction in order to effectu ate their promulgation. The rationale is on a basis so broad as t appear to encompass any kind of interstate communication and thu go beyond delegable powers of Congress. Congress can, of course delegate certain of its powers to the Commission, but inherent in such delegation is specification of adequate guidelines. The CATV rule making without congressional delegation of power but under jurisdic tion asserted by the Commission was, I believe, so lacking in requisit guidelines as to make it unconstitutional. 3 FCC 2d 827–829

V

MEMORANDUM OPINION AND ORDER IN DOCKET NOS. 14895, 15233 AND 15971, RM 1701 AND RM 1025, ADOPTED JANUARY 5, 1967

* * *

Dissenting Opinion of Commissioner Lee Loevinger

(On Reconsideration of CATV Rules, Dockets Nos. 14895, 15233, and 15971)

The Commission is now issuing an opinion and order in a group of related CATV rulemaking proceedings, the effect of which is to refuse to reconsider or change (except in some minor details) the CATV rules announced on February 15, 1966, and issued on March 8, 1966. In view of the probability of congressional consideration and action in the present session of Congress, this result is not unreasonable, and I would be inclined to concur were it not for the accompanying opinion. The opinion which the Commission is issuing is a typical institutional product which has had very slight Commission-level consideration or analysis. It is composed mainly of institutional cliches, but the implications of the reasoning now given Commission approval are sufficiently drastic and extensive to warrant more detailed analysis. My main objections are three:

First, the opinion asserts Commission jurisdiction which is self-bestowed and unlimited;

Second, the opinion fails to come to grips with either the issues or the facts and rests on semantic confusion and superstition;

Third, contrary to the express representations made by the Commission in this matter, the effect of the rules as now construed is to impose a freeze or prohibition on technological development and economic expansion in this field.

The position now taken by the Commission on jurisdiction is a prime example of lifting oneself by one's own intellectual bootstraps. Reduced to its barest elements this intellectual bootstrapping operation consists of asserting jurisdiction without statutory authority or precedent, refusing to hear argument regarding the position on the ground that the decision has already been made, and then proceeding to act on the jurisdiction asserted, pointing to one's own assertion and prior decisions as precedent and justification. If this characterization seems exaggerated, attention is invited to the actual course of events.

Federal regulation of radio transmission was instituted because "the radio spectrum simply is not large enough to accommodate everybody," radio transmitting stations were operating in such numbers and manner that there was chaos in the spectrum, and regulation of radio transmission was therefore "as vital to its development as traffic control was to the development of the automobile." *NBC* v. *U.S.*, 319 U.S. 190, 210–214 (1943). The Communications Act was passed in 1934 when television was still wholly experimental and CATV was unheard of. The basic function of the Commission and its basic authority, so far as relevant to this subject, was to license radio transmitting stations (47 U.S.C., sec. 151).

During the 1950's CATV and other ancillary television transmitting techniques developed and a demand was made that the Commission assert jurisdiction over them and regulate them. In 1958 the Commission instituted an overall "Inquiry Into the Impact of Community Antenna Systems, TV Translators, TV 'Satellite' Stations, and TV

'Repeaters' on the Orderly Development of Television Broadcasting," docket No. 12443. After a year of inquiry, the Commission issued an extensive report and order, finding, without dissent, that it was without jurisdiction over CATVs. *CATV and TV Repeater Services*, 26 FCC 403 (1959).

A few years later the Commission held that it was authorized to deny a license to transmit television signals by microwave radio transmission to a small community with one television station, on the ground that evidence of record showed that the economic impact of the applicant's operation would drive the television station out of business. *Carter Mountain Transmission Corp.*, 32 FCC 459 (1962), affd. 321 F. 2d 359 (C.A.D.C. 1963), cert. den. 375 U.S. 951 (1963). In *Carter Mountain* the Commission did not consider its own prior decision and its only comment on that precedent was: "To the extent that this decision departs from our views in * * * 26 FCC 403 * * * those views are modified."

The next step in the expansion of jurisdiction was the issuance of a "Notice of Inquiry" on April 23, 1965 (FCC 65-334). This was ostensibly an inquiry into whether the Commission had authority to promulgate rules regulating CATVs and particularly nonmicrowave CATVs (i.e., those transmitting signals wholly by wire and not employing radio transmission). However, attached to the "Notice of Inquiry" was a memorandum from the Commission general counsel asserting that the Commission did have plenary authority over CATVs "whether microwave is used or not." On the basis of this memorandum, without further discussion or inquiry, the "Notice of Inquiry" asserted the conclusion that "CATV systems are engaged in interstate communications by wire" and are, therefore, subject to the Commission's regulatory authority (FCC 65-334, par. 29). Neither the Commission's notice nor the memorandum on jurisdiction so much as mentioned the prior Commission determination that it lacked jurisdiction, and the memorandum relied wholly on general language in the Communications Act unrelated to either a specific grant of jurisdiction or the kind of action proposed by the Commission. See opinion of Commissioner Loevinger, 38 FCC 746. To no one's surprise, the Commission concluded this inquiry by reaching the decision that it did have jurisdiction to regulate cable CATV (i.e., systems not using any radio transmission) as well as microwave CATV. *Second Report and Order*, 2 FCC 2d 725 (1966).

A few months later in implementing its CATV rules the Commission issued a cease and desist order, the effect of which was to put a small town cable CATV out of business. *Back Mountain Telecable Inc.*, 5 FCC 2d 735 (1966). A demand was made for oral argument before the Commission on constitutional questions involved in this assertion of Commission jurisdiction. The Commission summarily denied this request on the ground that the views expressed in the *Second Report and Order*, supra, "dispose of the questions raised," and, hence, "no purpose would be served by oral argument," despite the fact that a dissenting opinion pointed out that not only did the opinion cited not "dispose of" the constitutional issues, but it did not even consider or mention them.

In the present opinion the Commission considers the constitutional free speech issue for the first time, with the statement that it will treat this question "in greater detail"—presumably meaning "greater detail" than the complete absence of discussion in prior opinions. However, the present discussion is confined to citing *NBC* v. *U.S.*, 319 U.S. 190 (1943), and *Lafayette Radio* v. *U.S.*, 345 F. 2d 278 (C.A. 2d 1965), for the proposition that "reasonable regulation of radio transmissions, if consistent with the public interest * * * is not violative of the right of free speech," and then concluding that:

> * * * there is no reason why the free speech principles should apply differently to those CATVs which derive their signals off-the-air than to those which use licensed radio.

The *Lafayette Radio* case sustained Commission regulation of Citizens Band radio on the grounds that the *NBC* case held licensing required by the limited facilities of radio. In the *NBC* case, the Supreme Court met the specific argument of constitutional free speech in these words:

> Freedom of utterance is abridged to many who wish to use the limited facilities of radio. Unlike other modes of expression, radio inherently is not available to all. That is its unique characteristic, and that is why, unlike other modes of expression, it is subject to government regulation. *NBC* v. *U.S.*, 319 U.S. 190, 226 (1943).

It should be self-evident from the Supreme Court statement that, contrary to the position of the instant opinion, there is every reason "why free speech principles should apply differently" to those CATVs which do not use radio transmission and to those which do. The whole reason and rationale for Government regulation in this field is the physical necessity for establishing and maintaining technical standards and order so that radio transmission is possible. Further, the rationale of the *NBC* case is based squarely and solely on the necessity of denying access to radio transmission to some because of the limited space in the spectrum. It makes no legal, technical, or logical sense to say that a case holding regulation to be justified because of the "limited facilities of radio" transmission, also justifies the same regulation of cable transmissions.

Furthermore, even the Commission opinions, when they have addressed themselves to the issue of jurisdiction, have based the conclusion of jurisdiction on the assertion that cable CATV is "engaged in interstate communication by wire" (FCC 65–334, par. 29)—on the theory that the signals carried have crossed a State line before being picked up by the CATV and transmitted by wire. But in the *Back Mountain* case a Pennsylvania CATV system was picking up Pennsylvania television stations and transmitting their signals by wire to its customers in Pennsylvania. (Some New York signals were also carried, but this activity was clearly separable for legal purposes.) The Commission has not yet seriously discussed or considered the legal basis of jurisdiction to order cessation of operation by a CATV system which picks up signals from a station within the State of its situs and transmits these by cable to customers in the same State. (The problem is brushed off by casual reference, without discussion, in a footnote in

the *Second Report*, 2 FCC 2d 732, footnote 9.) However, it ha entered cease and desist orders against such activities and has beer willing to order some such systems out of business. See, e.g., *Back Mountain Telecable, Inc.*, 5 FCC 2d 755 (1966).

Thus, the Commission has bootstrapped itself into an assertion o jurisdiction over all CATVs without ever squarely defining, analyz ing, and considering the issues, the legal basis of its jurisdiction, an the limitations of the jurisdiction asserted. By this intellectual boot strapping operation the Commission has moved from a specific stat utory authority to license interstate radio transmissions to the asser tion of a self-bestowed power to regulate and prohibit the intrastat transmission by wire of programs originating, broadcast, and receive within the same State. As authority the Commission relies on a Su preme Court opinion upholding regulation of interstate radio trans mission by licensing because of its unique characteristic and blandl asserts that there is no reason why the same principles should not appl to communication that is not by radio and that has entirely differen characteristics. As the jurisdictional issue has not yet been clearl defined, considered, or determined, it is by no means clear that ther is a majority of the Commission in support of the jurisdiction that i in fact being exercised, but so potent and impersonal is the bureau cratic institutional process that actions taken without definition o consideration of issues or principles become precedents which provid their own rationalization and finally preclude the Commission fron ever defining, considering, and thoughtfully determining their lega validity and implications.

The assertion of jurisdiction on such a basis as this should be matter of concern, but the underlying process and rationale and th implications for the future are even more important. The close the Commission has come to specifying a basis for the jurisdictio it is now exercising is in the *Second Report and Order*, 2 FCC 2 725 (1966). It there discusses jurisdiction as a matter of law (par 8–19), and assertion of jurisdiction (pars. 20–46). The argument under the first category boil down to the assertions that CAT systems "are themselves engaged in 'interstate communication b wire,'" and that there is no "bar to jurisdiction" (pars. 12, 19) Although the basis for asserting that CATVs are engaged in inter state communication by wire is not spelled out, it appears to rest o the fact that some CATVs receive radio broadcasts originating out side the State of situs and then transmit the programs thus receive over wires within the State of situs. The jurisdictional discussio under the second category is devoted entirely to the effort to sho that regulation of both microwave and cable CATV is subject t Commission regulation because "this is necessary in the public intere to avoid unreasonable competitive disadvantage and prejudicial effe on existing and potential television broadcast service * * *" (pa 21, et seq.).

If such reasons are adequate to support jurisdiction, then there no limit to the authority of this Commission. It is apparent at glance that these reasons apply with even greater force to the gre national television networks than to the CATVs. Yet the Commissio

has so far given no indication of the fact that it has often disclaimed jurisdiction to regulate networks, and has asked Congress for such authority, which has so far been withheld. If the present position of the Commission is sustained, the Commission has plenary power to control networks by direct regulation without any other or further legislative action. This conclusion is hinted, though not expressly claimed, in a footnote in the *Second Report*, 2 FCC 2d 732, footnote 9. Before this conclusion is accepted complacently, it should be noted that the asserted jurisdiction is now being exercised in the CATV field to require the carriage of some programs and to prohibit the carriage of others.

The implications of the jurisdiction now being asserted go much further. The reception of a program originating outside the State and its transmission to customers by wire is said to constitute interstate communication subject to regulation. If a program is put on tape or film and thus transported across a State line, then transmitted by wire to customers within a single State, all of the grounds urged for jurisdiction apply equally, and there is no logical basis for differentiating this mode of communication from that now subject to the asserted jurisdiction. If this is so, it seems immaterial to the considerations most relied on by the Commission whether the recorded program is exhibited by transmission intrastate to a number of houses or exhibited to the public in one or a few theaters. So, by this reasoning, the Commission has jurisdiction over motion picture theaters—to be exercised as the Commission in its wisdom decides that the economic consequences of motion picture exhibition require in the public interest.

By similar reasoning it can easily be demonstrated that most news and feature material in newspapers come to the publisher through interstate communication by radio or wire. (Very few modern newspapers still rely on the pony express.) But since the Commission in effect holds that the precise mode of presenting the interstate communication to the public is immaterial, the fact that pictures and words are printed on paper and then distributed after being transmitted interstate will not be controlling. The Commission can cite the *NBC* case for the proposition that the first amendment does not prevent reasonable regulation in the public interest. Next the Commission will assert that "there is no reason why the free speech principles should apply differently" to newspapers than to radio merely because the situation involving the technical mode of communication is different—and the instant opinion stands for just this proposition. Thus, by its present course of reasoning, the Commission has jurisdiction to regulate newspapers—in the public interest, of course.

With far less ingenuity and disregard of logic than has been demonstrated by the Commission's opinions thus far, the asserted jurisdiction can be extended almost literally without limit. If it be objected that this reasoning is strained and untenable—which it is—then it must be answered that, assuming validity of the Commission's present assertion of jurisdiction, the extensions suggested rest on more cogent and coherent reasoning than that by which the Commission reached its present position.

The Commission, of course, disavows any present intention o claiming jurisdiction over newspapers, theaters, and other media o communications or other enterprises. But only a few years ago, th Commission was just as positively disavowing the jurisdiction whicl it now asserts. It would take only a change of personnel or of view point—both of which are inevitable in time—for the Commission t assert the application of its self-bestowed jurisdiction to all mode of communication and entertainment.

I do not believe that Congress ever intended to grant or will i the future ever act to grant such a vague and limitless jurisdictio as the Commission now asserts and exercises. Even this cursor analysis should suffice to demonstrate that there is a strong prac tical, as well as legal, reason for insisting that the broad power o regulation should be confined within the jurisdiction specified b Congress in statutes, rather than left to be exercised at large by th hypothetical discretion of the institutional decision-making process

My second objection to the opinion is that it so clearly illustrate the most common inadequacy of the institutional decision-makin process. The opinion, like those that preceded it, simply fails t come to grips with either the issues or the facts and rests almos entirely on semantic confusion and superstition. The opinion sum marizes the provisions of the rules and the positions taken by th several petitions for reconsideration. Beyond this, the opinion re lies principally on the assertion that the results reached will serv the public interest. The public interest is referred to more tha 20 times, and serves as the main rationalization for the results reache regarding jurisdiction (pars. 4, 5, 8), regarding satellites (par. 10) regarding the use of grade B contours (pars. 13, 32, 33, 34), regardin nonduplication (par. 18), regarding the CATV freeze in major mar kets (pars. 23, 25), and regarding the use of grade A contours (par 30). The freeze in small markets, considered in more detail below is rationalized by invocation of the term "orderly" (par. 44).

It should take no great sophistication to understand that basin a decision on the bald assertion that it is required or implied b some high-order abstraction, such as "the public interest," "orderl procedure," or "the most desirable course," without specifying som concrete referents relevant to the case, is simply semantic super stition, equivalent to basing a decision on necromancy, astrology numerology, or tea leaf reading. It provides neither an explanatio of past actions nor a guide to future actions, and means no mor than that the decisionmaker has reached a result but cannot or wil not say why.

What constitutes a "private interest" in a given situation is ofte relatively clear—the monetary profit of an individual or corpora tion—although this term is not often used except as an ignoble con trast to the more honorific "public interest." But the public an private interests are by no means antithetical. On the contrary, it i the theory of our system that most often the public interest will con sist of allowing people to pursue their own private interests in thei own way. In any event, the "public interest" is not a single specifi criterion, a definite operational standard, or a term of self-evident

eaning. The most extensive and scholarly attempt to analyze the ncept of "public interest" comes to the conclusion that

> * * * our investigation has failed to reveal a statement of public-interest theory that offers much promise either as a guide to public officials who are supposed to make decisions in the public interest, or to research scholars who might wish to investigate the extent to which governmental decisions are empirically made in the public interest. For either of the latter purposes, it would be necessary to have operational definitions of the public-interest concept; and neither my analysis nor that of other contemporary critics suggests that the public-interest theory prevalent in America today either is or is capable of being made operational * * *. It may be somewhat difficult for some readers to accept the conclusion that there is no public-interest theory worthy of the name and that the concept itself is significant primarily as a datum of politics. As such, it may at times fulfill a "hair shirt" function, to borrow Sorauf's felicitous phrase; it may also be nothing more than a label attached indiscriminately to a miscellany of particular compromises of the moment. Glendon Schubert, "The Public Interest," 220, 223 (1960).

An analysis of the public-interest concept in the light of Supreme ourt decisions and in the context of Government regulatory power aches essentially the same conclusion. Loevinger, "Regulation and ompetition as Alternatives," 11 Antitrust Bulletin 101, 129 et seq. 1966). In upholding the concept as a criterion of action for the Comission, the Supreme Court was at pains to point out that it was "not be interpreted as setting up a standard so indefinite as to confer unmited power," but was to be interpreted by its statutory context, the ature of radio transmission and reception, and other factors. *NBC* v. *.S.*, 319 U.S. 190, 216 et seq. (1943). However, just as the Commision opinion has taken the Court's conclusion regarding the first amendent and applied it to precisely the kind of situation which the Court's pinion precludes by specific statement, so has it also taken the publicterest criterion and converted it into a "standard so indefinite as to onfer unlimited power." At no point in the instant opinion or any ther opinion is there any indication of the necessity of specifying hat the Commission conceives the public interest to mean in concrete erms in a particular situation. It uses the phrase "public interest" as nothing more than a label attached indiscriminately to a miscellany f particular compromises of the moment."

The instant opinion leaves the reader without a clue as to whether he phrase "public interest" as used in support of the decision has any eaning at all. Could it mean conservation of usable space in the pectrum? Clearly not—for the activities which are forbidden and imited by the rules tend to conserve spectrum, and the activities which re protected and encouraged use large amounts of spectrum. Could t mean minimizing or avoiding electronic interference? Clearly ot—for the activities which are forbidden and limited cause no interference, as they use no spectrum. Could it mean providing or encourging more diverse programs? Clearly not—for the best hope of teleision program diversity in many communities is probably through ATV, but the rules will favor a single television station over the iversity of a multichannel system if there is any economic conflict or ivalry between them. Does the public interest mean giving the public

what it wants or demands? Clearly not—for most of the rules and all of the cease and desist orders in this field are aimed at forbidding a service which a large segment of the local public is demanding and willing to pay for. Does the public interest mean to encourage experimentation and the development of new technology? Clearly not—for the principal purpose of the rules and the Commission actions under them is to limit and restrain the development of CATV as a new technology.

The only specific meaning that can be attributed to the phrase "public interest" as it is used in the Commission opinion is that it means protecting the private interest of broadcasters by limiting or suppressing any actual or potential competition by CATV.

Perhaps this objective can be justified in whole or in part. But it certainly has less sentimental appeal when plainly stated than when couched in the vague euphemism of "public interest," and also requires a good deal more by way of factual support, close examination, and logical analysis than the Commission has yet given the subject. Invocation of the pious phrase "public interest" may stir the emotions but it adds nothing to the intellectual argument and is merely a way of avoiding thought and cutting off debate. It does not have even the rationality of an appeal to divine guidance which was implicit in trial by compurgation, ordeal, and battle. To rest a conclusion on the justification that it "serves the public interest," without specifying concrete referents, is simply semantic superstition in contemporary terminology.

Finally, I object to the Commission's refusal to examine and consider the fact that the rules as now construed and in practical operation have imposed a freeze or prohibition on the development and extension of CATV service.

The CATV rules have been the subject of bitter controversy both in the industry and on the Commission since they were first proposed. In February 1966 the Commission met and the Commissioners agreed on a plan for the regulation of CATV systems which was set forth in a public notice dated February 15, 1966. This notice was not simply a press release but was the actual draft of the agreement among the Commissioners, and the text was carefully examined by the Commissioners as a precise statement of what the Commission had, in fact, agreed upon. This is made plain by the three statements accompanying the Commission notice, which state the personal concurrences and dissents on particular points of the Commissioners making the statements.

One of the principal purposes of the Commissioners in promulgating the February 15 compromise plan was to avoid a freeze on all CATV development and expansion, which had been previously urged upon them. This was done by providing in substance that in the top 100 television markets no CATV operation could be commenced or expanded without specific Commission approval, after a full evidentiary hearing and a finding that the potential effects of the proposed CATV operation would not be substantially competitive with any existing or proposed television stations, and that such an impediment would not be imposed outside the top 100 markets. On the latter point, the

specific language of the notice, which embodied the Commission action, was:

> The Commission's prior approval after an evidentiary hearing will not be required by rule for proposed CATV systems or operations in markets below 100 in the ARB rankings. However, the Commission will entertain, on an ad hoc basis, petitions from interested parties concerning the carriage of distant signals by CATV systems located in such smaller markets.

Three weeks later, on March 8, 1966, the Commission issued its institutional opinion and the text of the rules which were to effectuate the plan adopted February 15. The opinion and rules were more than 80 printed pages of small type (2 FCC 2d 725–808). The Commission issued another public notice announcing the adoption of these rules "to effectuate its plan for regulation of all CATV systems, as announced on February 15, 1966 * * *." The March 8 notice again summarized the provisions of the plan and the rules, and stated, in substantially the same language as on February 15, that (with exceptions immaterial here) no CATV operation could be commenced or expanded in the top 100 markets except with Commission approval after a full evidentiary hearing, and that no prior Commission approval or hearing would be required in smaller markets.

Since these rules were promulgated the institutional construction and application has converted the small-market rule into the equivalent of the rule applicable to the top 100 markets. That has occurred in this manner. The Commission plan, and the rules, provided that CATVs could commence or expand operation in the smaller markets without Commission approval but that any interested person could file an ad hoc petition in any situation and that the Commission could impose additional or different requirements than the rules (47 CFR, sec. 74.1109; 2 FCC 2d 725, 805). This has now been construed to mean that where a petition is filed to impose additional requirements upon, or prevent the operation of, a CATV system in a market smaller than the top 100, the CATV cannot commence or expand operations until it has a specific order of approval from the Commission. In plain language, the mere filing of a petition under section 74.1109 operates to impose an absolute and indefinite injunction against commencement or expansion of any operation by any CATV. Thus, any place and any time that there is any licensee, permittee, applicant, potential applicant, competitor, or other interested person who desires to stop the operation of a CATV system, he is given full power to do so by the present Commission rules. The mere filing of a petition, regardless of its form or merit and without any review or examination by the Commission, suffices to impose a complete prohibition against operation of the CATV system involved.

Thus, the compromise plan of February 15, which was adopted to avoid a freeze of CATV development, turns out to be a compromise in form and words only. No operation can be commenced or expanded in the top 100 markets until after the lengthy and arduous process of an FCC evidentiary hearing has been completed—which inevitably requires several years at least. No operation can be commenced or expanded in any other market if anyone objects. In the top 100

markets the freeze or prohibition operates automatically and regar less of objection. In all other markets the freeze or prohibition must invoked by some objection. But in practice there is no lack of o jectors. So the Commission has—albeit unintentionally and unkno ingly—in practical effect imposed a freeze on CATV development expansion in all markets, with only a slight procedural differentiati between the top 100 markets and the smaller markets, despite its e press disclaimers of such action in the public notices of February and March 8. This result the Commission now recognizes and affirn on the grounds that it is "more orderly" (par. 44). Needless to sa this verbalism is no more meaningful than the more favored "publ interest."

While I agree with Commissioner Bartley that the status quo this area is so unrealistic that it should be discarded, I might be i clined to concur in an opinion and order that did no more than mai tain the present rules on the ground that congressional action m be expected to provide guidance to the Commission in the near futur However, the present opinion has the form of a discussion of the merit but without factual or logical substance. The history of the develo ment of the Commission position on this subject, first as to jurisdicti and, more recently, as to the imposition of a general freeze, is su that no one can surmise, much less predict, from the semantic confusi and opacity of the instant opinion, what the Commission may do the future.

Perhaps the Commission should not attempt to regulate CATVs all. Perhaps the Commission should prohibit CATVs altogethe Perhaps the Commission should attempt to write some clear and co sistent rules to insure that CATVs will provide the public with bett and more diverse program service than the public would get in t absence of CATV. Perhaps a revision of the copyright law or section 325 of the Communications Act to give proprietary rights program originators is the best approach to this field. The only thin that is quite clear to me is that there is no hope of finding a ration and practical course until the Commission climbs out of the intelle tual morass and dispels the semantic fog in which this subject is no lost.

APPENDIX—B

Legislative History of Proposed Amendments to the Communications Act, Conferring Jurisdiction over CATV

I

After lengthy hearings on September 5, 1959, during the 86th Congress, First Session, the Committee on Interstate and Foreign Commerce submitted Senate Report 923 accompanying and recommending passage of Senate Bill S. 2653, entitled "A bill to amend the Communications Act of 1934 to establish jurisdiction in the Federal Communications Commission over Community Antenna systems." The bill provides as follows:

> That section 3 of the Communications Act of 1934 (47 U.S.C. 153) is amended by inserting at the end thereof the following: "(hh) 'Community antenna television system' means any facility performing the service of receiving and amplifying the signals transmitting programs broadcast by one or more television stations and redistributing such programs, by wire, to subscribing members of the public, but such term shall not include (1) any such facility which serves fewer than fifty subscribers, (2) any such facility which serves only the residents of one or more apartment dwellings under common ownership, control, or management, and commercial establishments located on the premises, or (3) any such facility used only for the distribution, by wire, of programs for which a charge is imposed generally on all subscribers wherever located and which are not in the first

instance broadcast for reception without charge by all members of the public within the direct range of television broadcast stations."

Sec. 2. Section 3 (h) of the Communications Act of 1934 (47 U.S.C. 153) is amended to read as follows:

"(h) 'Common carrier' or 'carrier' means any person engaged as a common common carrier for hire, in interstate or foreign communication by wire or radio or in interstate or foreign radio transmission of energy, except where reference is made to common carriers not subject to this Act; but a person engaged in radio broadcasting or in operating a community antenna television system shall not, insofar as such person is so engaged, be deemed a common carrier."

Sec. 3. Title III of the Communications Act of 1934 (47 U.S.C. 301 and the following) is amended by inserting therein a new section 330 as follows, entitled:

"COMMUNITY ANTENNA TELEVISION SYSTEMS

"Sec. 330. (a) No person shall operate a community antenna television system except under and in accordance with this Act and with a license granted under the provisions of this Act: *Provided*, That a Community antenna television system which is in operation on the date of the enactment of this section may continue to operate until the Commission issues a license therefor: *Provided further*, That any system continuing to operate in accordance with the foregoing shall, not later than one hundred and twenty days after such enactment, submit an application for a license containing all the information required by the Commission to be submitted with such application.

"(b) (1) The provisions of sections 303, 304, 307, 308, 310, 311, 312, 313, 315, and 316 relating to stations, radio stations, broadcasting stations, licenses therefor, licensees thereof, and station operators shall apply also to community antenna television systems, licenses therefor, licensees thereof and operators thereof.

"(b) (2) The provisions of section 317 relating to matters broadcast by any radio station, and section 326 relating to radiocommunications shall be deemed to apply also to all matter distributed to its subscribers by a community antenna television system.

"(b) (3) The provisions of section 319 relating to construction permits shall apply also to the construction and licensing of a community antenna television system: *Provided,* That the Commission, if it finds that the public interest, convenience and necessity would be served thereby, may waive the requirement of a permit for such construction.

"(c) The public interest, convenience, and necessity will be deemed to be served by the grant of an application for a license for the provision of existing program services by a community antenna television system which was in operation on the date of the enactment of this section subject to such conditions as the Commission may impose under subsection (d) hereof.

"(d) (1) Either prior to or within thirty days after the grant of an application for a license or a renewal thereof for a community antenna television system which was in operation on the date of the enactment of this section, the licensee of a television station assigned to a community in which such community antenna television system serves subscribers may petition the Commission to include in such license such conditions on the community antenna television system's operation as will significantly facilitate the continued

operation of a television station which is providing the only available locally originated television broadcast program service.

"(d) (2) Such petition shall describe, in detail, the proposed operating conditions, and shall set forth, with particularity, the material effect of the proposed conditions on such continued television station operation. The community antenna television system shall be afforded an opportunity to respond to such petition within thirty days after public announcement of the filing thereof. After the expiration of such thirty-day period, the Commission shall determine whether the petition meets the foregoing requirements, and, if it does, shall determine whether, with due regard to service rendered by the community antenna television system and by petitioner's station, the public interest, convenience and necessity would be served by the adoption of the proposed or any other operating conditions. Public evidentiary hearings shall be held thereon if requested by either the petitioner or the community antenna television station within thirty days after public ammouncement of such determination, or if ordered by the Commission on its own motion prior to its determination.

"(d) (3) Any community antenna television system license issued under subsection (c) above shall be subject to conditions imposed in accordance with this subsection but any such license so issued shall not be stayed pending the Commission's final decision on any petition filed hereunder.

"(e) Findings by the Commission as to the effect upon the public interest, convenience, and necessity of the grant of an application or renewal or modification *thereof* for a community antenna television system which was not in operation on the date of

the enactment of this section or for modification of a license for a community antenna television system which was in operation on the date of enactment of this section shall be made with due regard for the desirability of facilitating the continued operation of a television station which is providing the only available locally originating television broadcast program service. The provisions of section 309 shall apply to the issuance of licenses, modifications, and renewals thereof under this subsection.

"(f) (1) Upon application by the licensee of a television broadcast station (other than a station engaged solely in rebroadcasting) which is assigned to a community in which a community antenna television system provides television programs to local subscribers, the Commission may require that such community antenna service shall regularly redistribute programs broadcast by such local television broadcast station.

"(f) (2) The Commission may, by rule or order, prescribe such standards and conditions as it may find necessary to assure that the reception of the programs redistributed by the community antenna television system under subsection (1) shall be reasonably comparable in technical quality to the reception of programs of other television stations redistributed by the community antenna television system.

"(f) (3) The Commission also may, by rule or order, prescribe the period of time within which community antenna television systems shall complete preparations for and commence the redistribution of programs under subsections (1) and (2).

"(g) The Commission shall prescribe appropriate rules and regulations in order to avoid the duplication of programs broadcast or scheduled to be broadcast

by a television station (other than a station engaged solely in rebroadcasting) which is assigned to a community in which a community antenna television system serves subscribers by such communtiy antenna television system redistributing the signals of another television station. In promulgating such rules and regulations the Commission shall be guided by the standard set forth in subsection (e) of this section, requiring that due regard be given for the desirability of facilitating the continued operation of a television station which is providing the only available locally originating television broadcast program service."

The Committee report explained the purpose of the bill was to place CATV under the jurisdiction of the FCC.

> This bill is designed to amend the Communications Act of 1934 so as to place community antenna television systems (CATV) under the jurisdiction of the Federal Communications Commission and to empower the Commission to issue requisite certificates of public interest, convenience, and necessity for the construction and operation of community antenna television systems. This bill declares CATV systems not to be common carriers and sets forth the sections of title III of the Communications Act affecting regular broadcasters that are to apply to the community antenna television systems.
>
> (Senate Report 923, p. 3)

The Report summarized the Commission's treatment of CATV since its inception and referred to its disclaimer of jurisdiction in *Frontier Broadcasting v. Collier*, 16 Pike and Fischer R.R. 1005 (April 1958).

> The question of the FCC's jurisdiction over community antenna television systems and the type of

> regulation that should be imposed was raised many years ago. The FCC's files make it clear that this issue was presented to it as early as 1950 and that its staff recommended that it exert authority in this field. But, the Commission has long hesitated over the matter. In speeches by individual commissioners and in testimony before your committee, doubt as to its power has been expressed but no official ruling was made until April 21, 1958, when the FCC decided a long-pending proceeding instituted by a group of small-town broadcasters who asked that the Commission regulate CATV systems as common carriers. (*See Frontier Broadcasting Company v. Collier,* 16 R.R. 1005 (April 1958). The Commission's final action in this matter made it perfectly clear that it did not intend to regulate CATV systems in any way whatsoever. However, on May 22, 1958, the FCC instituted an inquiry into the impact of community antenna television systems, television translators, television satellite stations, and television reflectors upon the orderly development of television broadcasting (docket No. 12443) and included as part of that proceeding the reconsideration of the above-mentioned *Frontier Broadcasting* case. (Senate Report 923, p. 5)

After several amendments to the bill were offered, S. 2653 was debated on the Senate floor on May 17 and 18, 1960. Senator Pastore, chairman of the sponsoring committee, was the floor leader and explained that the bill was not designed to hurt CATV, but merely place it under regulatory control:

> This bill is not directed in any way toward injuring CATV as such. We seek merely to place CATV systems under regulation in order to protect their rights, and also to protect the rights of the only available broadcasting station, which may perish and go out of

existence unless proper reforms are taken now of a
very moderate nature.
(106 Cong. Rec. 10417)

Senator Pastore was questioned at length on the purposes of the bill and explained it was a new delegation of authority of jurisdiction over CATV. In a brief colloquy Senator Pastore stated:

> Mr. CURTIS. First, I thank the distinguished Senator for his long efforts in a difficult area. I have given very limited study to S. 2653. It appears to me that the proposed legislation places the community antenna systems under the jurisdiction of the Federal Communications Commission. To that extent there is a delegation of authority to them. Does the bill directly prohibit or outlaw any act that the community antenna systems are doing now?
>
> Mr. PASTORE. I do not think so, aside from the fact that now they are at liberty to take a picture from a broadcasting station in Phoenix and show it in Yuma, for example. It may be earlier than the picture would be shown on the local broadcasting station in Yuma, and if the broadcasting station at Yuma made an application to the FCC, it could bring that to a stop. That would be a deprivation of some activity. That is about as far as it would go.
>
> Mr. CURTIS. The bill grants to the Commission the right to look into that situation?
>
> Mr. PASTORE. And to make rules and regulations.
>
> Mr. CURTIS. To make rules and regulations.
>
> But in the absence of action by the Commission, is there anything in the bill which prohibits what the community antenna systems can do?
>
> Mr. PASTORE. I would not say so, unless the Senator sees something in the bill to the contrary.
> (106 Cong. Rec. 10425)

In answer to questions by Senator Kerr, an opponent of the bill and the grant of jurisdiction to the FCC over CATV, Senator Pastore explained that the jurisdictional grant was necessary to develop an orderly system of TV:

> Mr. PASTORE. Then it is necessary to put these people under regulation, so that as new licenses are granted the Federal Communications Commission will have jurisdiction. The FCC then will be in a position to develop an orderly system of TV. However—and this must be borne in mind—insofar as harassment is concerned, or so far as a burden may be incurred, because of the duties that are imposed upon a CATV organization where there is no problem, I would assume the action of the Federal Communications Commission would be nothing more than perfunctory. (106 Cong. Rec. 10426)

The Kerr-Pastore debate demonstrated that the issue before the Senate was whether the FCC was to gain jurisdiction over CATV through the passage of the amendment—jurisdiction which it admittedly lacked:

> Mr. KERR. Did it ever occur to the Senator from Rhode Island that there are hundreds and thousands of American businesses in operation who are praying unto the Lord and their Government to protect them by keeping them free of regulation, rather then imposing it on them and then having them depend upon a legislative record made on the floor of the Senate which, if someone downtown whose identity we do not know, is controlled by it, will let them loose after they have paid a bunch of lawyers in Washington to come down to get them loose?
>
> The Senator says he cannot write a bill to protect these people. Apparently the Senator does not know his own ability. * * *

> Mr. PASTORE. There was not one representative of a CATV who appeared before our committee who did not say that he wanted to be regulated. I call as my chief witness the Senator from Oklahoma [Mr. MONRONEY], who is going to make the motion to recommit the bill. As a matter of fact, Senator MONRONEY introduced a bill himself to regulate the entire industry. However, that bill is only a shell. It does put them under regulation, but it does not regulate.
>
> Mr. KERR. Next to not being under it, that is the best shape one can be in.
>
> (106 Cong. Rec. 10426)

Senator Pastore urged that by conferring jurisdiction over CATV, the bill would actually provide protection to CATV systems against exorbitant charges by the broadcast station, should the stations prevail in pending copyright litigation. Senator Kerr countered that the FCC through its present jurisdiction over the broadcasters could protect CATV without extending its jurisdiction to CATV.

> Mr. KERR. Did the Senator from Rhode Island say the Federal Communications Commission, which has control of the station whose signal is being picked up, could not control them without this act?
>
> Mr. PASTORE. I did not say that.
>
> Mr. KERR. That is what the Senator did say.
>
> Mr. PASTORE. I said the CATV would not have any right to go before the FCC.
>
> Mr. KERR. Who says they would not?
>
> Mr. PASTORE. I say so.
>
> Mr. KERR. Who prescribes that?
>
> Mr. PASTORE. Because the Senator says they should be put under the CATV. That is just the point.

Mr. KERR. Cannot a person go into court and ask for justice, without being set aside by the court?

Mr. PASTORE. The FCC is not a court. It is a regulatory body. We are trying to put the parties under this body with appropriate procedures.

Mr. KERR. The Senator wants to make them slaves, without provision for protection of their lives. How silly can one get?

Mr. PASTORE. I am not silly. I am talking about jurisdiction.

Mr. KERR. So am I.

Mr. PASTORE. I am talking about jurisdiction, and there is nothing silly in it.

Mr. KERR. The Federal Communications Commission does not have to be given regulatory control over any citizens to enable those citizens to go before that Federal Communications Commission and file a petition.

Mr. PASTORE. A petition to do what?

Mr. KERR. To enforce any right that an American citizen has with reference to that Commission's jurisdiction.

Mr. PASTORE. The Senator could not be more wrong than he is.

(106 Cong. Rec. 10429)

Senator Pastore, the floor manager, insisted that the bill was necessary to confer CATV jurisdiction upon the FCC, and that without it, the Commission was powerless to act.

Regarding the effects of the bill in conferring jurisdiction, Senator Monroney emphasized that it would provide unprecedented economic protection to broadcasters.

The only test for the granting of a license for a television or a radio station, in the long history of the Federal Communications Act, has been, Is there a frequency

available which will not interfere with the frequency assigned to someone else? A hundred television stations could be established if frequencies were available for them. If there is a radio station in Yuma, six stations could be put in if frequencies could be found for them. But we have never contemplated granting economic protection to licensees until this bill was introduced. We are breaking entirely new ground, which will extend in the future to such a point that other people will want to install television in an area, and it will be necessary to provide economic protection for the local single station. I do not think such a policy has ever been established.
(106 Cong. Rec. 10535)

Senator Monroney compared the immunity from FCC regulation of reception and cable distribution by CATV to that enjoyed by the television networks:

Mr. LONG of Louisiana. Does the bill violate the principle that the airways are free and are available to everyone?

Mr. MONRONEY. I do not think it does. But it violates the principle of not having Federal regulation of cable transmission.

Let me state the best illustration: All of us know that the mightiest force in television, which controls 90 percent of all television programs received by viewers in the United States, are the networks. They are not subject to regulation, and very few Members of Congress would want them to be regulated. Why? Because the concept of the Federal Communications Act is that the networks themselves are not putting anything on the air. They use cables to carry the signals to the local stations. So they are not regulated.

So we do not regulate—and I do not think we should—the mighty giant of television which supplies the television diet of 50 million television sets by carrying the television program signals by cable to the viewers.

But if the quite similar CATV systems are to be regulated by means of this bill, we shall be establishing a precedent; and in that event I do not see how we can properly regulate the smallest midget in the industry, but fail to give some consideration to regulating the mighty networks which are carrying signals by means of a similar system, and also without using the airways. (106 Cong. Rec. 10536)

Senators opposing the amendment recognized that the bill was designed to provide economic protection for television.

Mr. McCLELLAN. The meaning of the word "facilitate," as I understand it, is to make easy or less difficult; to free from difficulty or impediment. In other words, it is to facilitate the execution of a task; to lessen the labor of; to assist; aid.

In other words, the station owner could petition the Federal Communications Commission to impose conditions that will facilitate, that will aid, that will remove any difficulty, that will remove encumbrance or hindrence to the continued operation of that station.

Mr. MONRONEY. Which would mean limiting competition, which this bill is designed to do, from newly constructed CATV's.

* * *

Mr. McCLELLAN. In other words, the rules the Commission promulgates must be promulgated to achieve that purpose. That is the proposed law we are considering. I am not saying it is not a good thing,

> but I think we ought to know what it does. This provision sets up a TV station in a position of preferred consideration, and in a position of preferred consideration in competition with another station.
> (106 Cong. Rec. 10537)

Senator Long registered concern over the economic advantage to broadcasters conferred by the bill.

> Mr. LONG of Louisiana. I am referring to page 4 of the bill, at line 21, where it provides:
>
> A television station * * * may petition the Commission to include in such license such conditions on the community antenna television system's operation as will significantly facilitate the continued operation of a television station which is providing the only available locally originated television broadcast program service.
>
> The thought that occurs to me is that it would seem to go far enough to say that the community antenna system should not impose any undue injury of hardship on the television station. However, to say that it could be required to operate in a manner to facilitate the continued operation of the competitor and system in his business, is too much to ask.
>
> * * *
>
> Mr. LONG of Louisiana. As the law stands today there is nothing in the law by which the FCC can prevent one television station from driving another one out of business. I have seen that happen in my state, where a VHF station came into the community which had a UHF station, by providing a better signal and better programs.
> (106 Cong. Rec. 10541)

Senator Hickenlooper questioned whether the proposed amendment conferring jurisdiction upon FCC was constitutional.

> Mr. HICKENLOOPER. Mr. President, I merely wish to ask some questions of the Senator from Oklahoma or of another Member of the Senate.
>
> It seems to me that a rather conplicated legal situation could arise in this instance. As I understand, a CATV station merely takes something out of the air, and does not put anything into the air.
>
> Mr. MONRONEY. That is correct.
>
> Mr. HICKENLOOPER. After it takes something out of the air–just like using the air we breathe–it then wires it, by means of a physical operation, into a house, where it is hooked up to a television set.
>
> Mr. MONRONEY. That is correct.
>
> Mr. HICKENLOOPER. What justification is there for having the Federal Government move into that regulatory field? Can it be called interstate commerce? If so, can the Federal Government then regulate my radio set in my house because I take the signal out of the air by means of an aerial erected on top of my house?
>
> Mr. MONRONEY. This presents a problem, because many think this is exclusively in the field of interstate commerce. Of course, the ether waves are interstate. But when the signal is taken out of the air and is transmitted to the Senator's house by cable, that is purely intrastate.
>
> (106 Cong. Rec. 10543)

The issue to recommit the bill was plainly and openly acknowledged as an attempt to defeat it.

> Mr. KERR. Mr. President, I rise in support of the motion to recommit the bill. I do it for the simple reason that I think it is an absolute necessity to protect the well-being and the opportunity for existence of over 760 small businesses.
> (106 Cong. Rec. 10544)

The bill was recommitted by a vote of 39 to 38, 106 Cong. Rec. 10547. A vote to reconsider failed 38 to 36. As a post mortem to the defeat of S. 2653, Senator Moss, a proponent of the bill, asked for further study by Congress as to whether, in view of the bill's failure to pass, appropriate legislation should be enacted to grant the FCC some jurisdiction over CATV in order to protect local television.
(106 Cong. Rec. 11462)

Throughout the lengthy debate, both proponents and opponents assumed that the legislation was necessary in order to confer jurisdiction upon the FCC over CATV. The legislation failed to pass.

II

On February 22, 1961 in the 87th Congress, 1st Session, S. 1044 was introduced, entitled "a bill to amend the Communications Act of 1934 to authorized the Federal Communications Commission to issue rules and regulations with respect to community antenna television systems." Placed in the record was an explanatory statement prepared by the Commission, which states in part:

> In examining into this matter the Congress considered numerous legislative proposals and held hearings thereon. Two of these proposals, S. 2653 and H. R. 11041, would have established a broad-scale and mandatory licensing scheme for the some 500-700 community antenna television systems which are already in existence, as well as those proposed to be established in the future. While the Commission was in accord with

the general objective of these bills, it expressed the view that they were unnecessarily comprehensive in scope; would reach into situations which did not affect local television stations; and would unnecessarily add to the already large licensing functions of the Commission.

In contrast to the unduly widespread scope of these bills, the instant proposal is designed to vest in the Commission authority to act in those situations where local television stations are operating under inequitable disadvantages in competition with community antenna television systems. The Commission would thereby be enabled to address itself to the problem situations in the CATV-local station areas under a general power to make appropriate adjustments through the issuances of appropriate rules, regulations, and orders. The Commission would not, however, be encumbered by the administration of a mandatory licensing scheme for community antenna television systems, including the large number of such systems which are providing the only television service to sparsely settled areas.
(107 Cong. Rec. 2524)

* * * * *

Another instance of the way in which the Commission's jurisdiction might be exercised in appropriate situations lies in the field of duplication by CATV systems of programs being carried by the local station. The Commission would be empowered under the proposed legislation to order such adjustments as would, on an appropriate basis, permit the CATV system to continue to provide multiple television services, and at the same time afford to the local station some protection in its program offerings.

Since this legislative proposal looks to a limited jurisdiction over CATV's under the Communications Act of 1934, as amended, the enforcement and review

> provisions in section 312 (b) and titles 4 and 5 of the act would be available in connection with rules, regulations, and orders issued by the Commission with respect to CATV operations. (107 Cong. Rec. 2524)

Implicit in this memorandum is the understanding that such legislation was necessary in order to authorize the Commission to promulgate rules and regulations over CATV.

III

In the 89th Congress, S. 3017 was introduced on March 4, 1966, 112 Cong. Rec. 4689. [1] It was entitled "a bill to amend the Communications Act of 1934 to authorize the Federal Communications Commission to issue rules and regulations with respect to community antenna systems, and for other purposes." The bill provided no regulatory scheme or rules as did S. 2653, but merely conferred jurisdiction over CATV upon the FCC. It also barred program origination by CATV, and relegated it to the role of receiving and distributing broadcast signals. This bill was submitted subsequent to the FCC's assumption of jurisdiction and was designed, in the words its chairman, a confirmation of jurisdiction.

> The Commission had determined that it has jurisdiction over all CATV systems, and it has asserted that jurisdiction to the extent necessary to carry out the announced regulatory program. However, given the importance of CATV, we believe it highly desirable that Congress amend the Communications Act to confirm that jurisdiction and to establish such basic national policy as it deems appropriate.

* * *

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[1] Citations to pages from the 89th Congress are to the daily edition, since the permanent edition is not yet available.

Of prime importance is the proposed new section 331(a)(1) of the act, which would expressly confer upon the Commission, in broad and comprehensive terms, authority to regulate community antenna systems in the public interest. This authority is to be exercised only to the extent necessary to carry out the purposes of the Communications Act, particularly the establishment and maintenance of broadcast services and the provision of multiple reception services. There is thus a congressional recognition of the public service rendered by the broadcast and CATV industries and a directive to promote the orderly growth of both industries. (112 Cong. Rec. 4690)

Also, submitted along with the explanatory statement is the dissenting statement of Commissioner Loevinger who adhered to the previous FCC rulings that it had no jurisdiction.

SEPARATE STATEMENT OF COMMISSIONER LEE LOEVINGER REGARDING PROPOSED CATV LEGISLATION

I believe it is necessary for Congress to legislate on the subject of community antenna television and that the draft of proposed legislation submitted herewith by the FCC is the best compromise that can now be agreed upon. It is my opinion that under present statutes the Commission does not have the jurisdiction which it claims over CATV's. See my separate opinion at 4 R R 2d 1679, 1712. If the Commission is to act in this field, legislative authorization is, therefore, necessary.

* * *

It would be desirable for Congress to establish more specific standards for administrative action than are contained in the proposed bill. But it is appropriate for Congress to delegate broad authority for the Commission to act under whatever standards Congress may see fit to establish.

Accordingly I join in recommending that Congress consider the proposed bill submitted herewith and enact legislation in such form as may best express the congressional view of the proper way to deal with the problems involving FCC jurisdiction to regulate CATV systems, the operation of CATV systems, the relations of CATV systems to conventional broadcasting stations, and the relation between Federal and State jurisdiction in this field.
(112 Cong. Rec. 4691)

The bill S. 3017, contains the following language:

"That section 3 of the Communications Act of 1934 (47 U.S.C. 153) is amended by adding at the end thereof a new subsection to read as follows:

"(gg) 'Community antenna system' means any facility which, in whole or in part, receives directly or indirectly over the air and amplifies or otherwise modifies the signals transmitting programs broadcast by one or more broadcast stations and distributes such signals by wire or cable to subscribing members of the public who pay for such service."

SEC. 2. The Communications Act of 1934 is further amended by adding a new section to read as follows, entitled:

"COMMUNITY ANTENNA SYSTEMS"

SEC. 331. (a) The Commission shall, as the public interest, convenience or necessity requires, have authority:

"(1) to issue orders, make rules and regulations and prescribe such conditions or restrictions with respect to the construction, technical characteristics, and operation of community antenna systems, to the extent necessary to carry out the purposes of this Act, with due regard to both the establishment and maintenance of broadcast service and the provision of multiple reception services;

"(2) to make general rules exempting from regulation, in whole or in part, community antenna systems where it is determined that such regulation is unnecessary because of the size or nature of the systems so exempted.

"(b) No community antenna system shall transmit over its system any program or other material other than that which it has received directly or indirectly over the air from a broadcast station, except that the Commission may, upon an express finding that it would serve the public interest, authorize by general rule limited exceptions to permit such transmissions without any additional charge to subscribers.

"(c) Nothing in this Act or any regulation promulgated hereunder shall preclude or supersede legislation relating to, or regulation of, community antenna systems by or under the authority of any State

or Territory, the District of Columbia, the Commonwealth of Puerto Rico or any possession of the United States except to the extent of direct conflict with the provisions of this Act or regulations promulgated hereunder."

IV

Again in the 89th Congress 2d Session a bill was introduced conferring jurisdiction over CATV. On June 17, 1966 the House Committee on Interstate and Foreign Commerce issued Report No. 1635, accompanying H.R. 13286, entitled "a bill to amend the Communications Act of 1934 to authorize the Federal Communications Commission to issue rules and regulations with respect to community antenna systems, and for other purposes." The bill, as amended, provides:

> That (a) section 3 of the Communications Act of 1934 (47 U.S.C. 153) is amended by adding at the end thereof the following new subsection:
>
> "(gg)'Community antenna system' means any facility which, in whole or in part, receives directly or indirectly over the air and amplifies or otherwise modifies the signals transmitting programs broadcast by one or more broadcast stations and distributes such signals by wire or cable to subscribing members of the public who pay for such service."
>
> (b) Subsection (h) of such section 3 is amended to read as follows:
>
> "(h) 'Common carrier' or 'carrier' means any person engaged as a common carrier for hire, in interstate or foreign communications by wire or radio or in interstate or foreign transmission of energy, except where

reference is made to common carriers not subject to this Act; but a person engaged in radio broadcasting or in operating a community antenna system shall not, insofar as the person is so engaged, be deemed a common carrier."

SEC. 2 Part I of title III of the Communications Act of 1934 is amended by adding at the end thereof the following new section:

"COMMUNITY ANTENNA SYSTEMS"

"SEC. 331. (a) The Commission shall, as the public interest, convenience or necessity requires, have authority —

"(1) to issue orders, make rules and regulations, and prescribe such conditions or restrictions with respect to the construction, technical characteristics, and operation of community antenna systems, to the extent necessary to carry out the purposes of this Act, with due regard to both the establishment and maintenance of broadcast services and the provisions of multiple reception services; and

"(2) to make general rules exempting from regulation, in whole or in part, community antenna systems where it is determined that such regulation is unnecessary because of the size or nature of the systems so exempted.

The Commission shall, in determining the application of any rule or regulation concerning the carriage of local broadcast stations by community antenna systems, give due regard to the avoidance of substantial disruption of the services to subscribers of community antenna systems which were in operation on

March 1, 1966, resulting from the limited channel capacity of any such systems.

"(b) No community antenna system shall transmit over its system any program or other material other than that which it has received directly or indirectly over the air from a broadcast station, except that the Commission may, upon an express finding that it would serve the public interest, authorize by general rule limited exceptions to permit such transmissions without any additional charge to subscribers.

"(c) The Commission shall prescribe such rules and regulations and issue such orders as may be necessary to require the deletion by community antenna systems of signals carrying any professional football, baseball, basketball, or hockey contest if, after application by the appropriate league, the Commission finds that the failure to delete such signals would be contrary to the purposes for which the antitrust laws are made inapplicable to certain agreements under Public Law 87-331.

"(d) Nothing in this Act or any regulation promulgated under it shall preclude or supersede legislation relating to, or regulation of, community antenna systems by or under the authority of any State, the District of Columbia, the Commonwealth of Puerto Rico, or any possession of the United States except to the extent of direct conflict with the provisions of this Act or regulations promulgated under it."

In the purposes of the legislation the Committee was cautious not to challenge the FCC's already assumed jurisdiction.

> The principal purposes of the legislation are to —
>
> (1) delineate the scope of the authority of the Federal Communications Commission to regulate CATV systems. (H. R. Rep. No. 1635, p. 2.)

The Committee pointed out that although the Federal Communications Commission had asserted its jurisdiction over CATV, the Committee would not state a position, except to say that the Congress should confer this jurisdiction.

> In reporting the instant legislation, the committee does not either agree or disagree with the above conclusions. Test cases are pending at present in the courts. Therefore, the question of whether or not and to what extent the Commission has authority under present law to regulate CATV systems is for the courts to decide in such cases.
>
> It is the considered judgment of the committee, however, that in order properly to regulate broadcasting and communications in the United States the Commission should have the broad powers which the instant legislation would confer upon the Commission to regulate CATV systems. (H. R. Rep. No. 1635, p. 9)

The Commission, in its explanatory note attached to the Committee report, candidly admitted it wished the Congress to confirm jurisdiction which it had assumed.

> The Commission has determined that it has jurisdiction over all CATV systems, and it has asserted that jurisdiction to the extent necessary to carry out

> the announced regulatory program. However, given the importance of CATV, we believe it highly desirable that Congress amend the Communications Act to confirm that jurisdiction and to establish such basic national policy as it deems appropriate. (H.R. Rep. No. 1635, p. 16)

Commissioner Loevinger issued a separate statement explaining that although he favored the proposed legislation, he believed it necessary to confer jurisdiction upon the FCC.

> I believe it is necessary for Congress to legislate on the subject of Community Antenna Television and that the draft of proposed legislation submitted herewith by the FCC is the best compromise that can now be agreed upon. It is my opinion that under the present statutes the Commission does not have the jurisdiction which it claims over CATV's. See my separate opinion at 4 RR 2d 1679, 1712. If the Commission is to act in this field legislative authorization is, therefore, necessary. (H.R. Rep. No. 1635, p. 20)

The Department of Justice, in response to a request for its views, was careful not to state an opinion as to whether the FCC had jurisdiction over CATV.

> The principal purpose of the bill is to clarify and confirm the Commission's jurisdiction over community antenna systems in order that the Commission shall have clear authority to integrate community antenna service into the national broadcast structure in such a way as to promote maximum service to everyone, including both those

> persons who are dependent upon off-the-air service and those who may receive cable service.
> (H.R. Rep. No. 1635, p. 21)

The minority report of the Committee did not hesitate to state its position that the Commission lacked jurisdiction over CATV and that the Commission had unlawfully usurped this jurisdiction.

> H.R. 13286 is a bill that was prepared by the Federal Communications Commission and forwarded to the Congress with the request that it be passed. It is not an administration bill. It is an attempt by a Federal agency to force Congress to give its jurisdiction which it heretofore claimed it did not have. The passage of this bill at this time would serve to underwrite an unauthorized assumption of jurisdiction by the Federal Communications Commission; it would thwart the judicial processes which are presently considering the issues involved; it would create an entirely new concept of regulation at Federal level; it would violate the constitutional guarantees of the first amendment; it would permit a Federal administrative agency (supposedly an arm of the Congress, created by the Congress) to write substantive law by the exercise of rulemaking powers; it would authorize a Federal agency, not answerable to the electorate, to repeal the laws of the several States by rulemaking powers; it would authorize monopolistic practices in the broadcasting of professional sports events and deny millions of people the opportunity of witnessing these events by television; it would create the power of censorship in the Federal Communications Commission insofar as CATV systems are concerned; it would give the Federal Communications Commission the authority in certain areas to determine what a

person could or could not receive over his television or radio set—to name a few of the flaws.

Television and radio were not intended to be regulated in the same manner as public utilities. They were subjected to regulation only because of the limited frequencies available in the spectrum. Regulation was for the sole purpose of properly policing the spectrum and seeing that it was not abused. Hence, licenses for broadcasting radio signals were required, because the spectrum was public domain and subject to the police powers of the sovereign.

The history of the Communications Act of 1927 and the amendments thereto of 1934 reflects clearly that the purpose of regulation was to make it possible for the full spectrum to be used in an orderly manner so that broadcast signals would not conflict with each other and thereby create a pandemonium of static which would be of no use to anyone. The operation of the businesses operating under licenses issued by the Government was to be on the free enterprise base. In other words, it was spelled out in the history that the Government would not have jurisdiction of the economics of the several broadcasters. Whether or not they were able to stay in business or to be successful in their operations was to be determined solely by the traditional free enterprise system upon which this country was built. Many attempts have been made by the Federal Communications Commission to gain economic control over the broadcasters. The most recent attempt was in 1963 when the Commission issued orders limiting the length and frequency of broadcast commercials. The House of Representatives struck down this

attempt by the passage of a bill denying them the power to enter the field of economic control.

H.R. 13286 as proposed by the Federal Communications Commission is an attempt to gain economic control over CATV systems and thence to move forward to gain economic control over broadcasters and thereby measurably expand the regulatory powers of the Communications Commission on a Federal basis.

A CATV system is a wired communications system and does not use the spectrum or public domain for broadcasting pruposes. Hence, the Commission has heretofore held on several occasions that it did not have jurisdiction of CATV systems as such.

There are three methods by which programs can be received by a CATV system to be transmitted over its wires:

1. The pure off-the-air system. This is the case where a high antenna is employed to catch any broadcast signals that happen to come its way.

2. The microwave-fed system. This is the system where the original broadcast is rebroadcast through the spectrum, one or several times, until it reaches its desired destination. (The FCC has jurisdiction over the microwave facility because it is a rebroadcast into the spectrum, but not over the reception facility.)

3. The coaxial cable. This is a system where a coaxial cable is employed from the broadcasting station to the CATV system. If the coaxial cable does not cross a State line, the Federal Communications Commission does not have jurisdiction. If the coaxial cable does

> cross a State line, the jurisdiction of the FCC attaches under its jurisdiction over an interstate common carrier by wire. However, in this case the jurisdiction of the Commission does not extend to a determination of what can or cannot be carried over the wire.

The present bill is designed to give the Federal Communications Commission absolute control over reception by all three methods. The main objective of the Federal Communications Commission is to gain control ofer the off-the-air (subpar. 1 above) and the coaxial cable (subpar. 3 above), for by this method the Commission can gain direct control over reception of television signals insofar as all CATV systems are concerned. It has had an indirect, limited power over CATV systems using microwave. The operator of a microwave facility must get a license from the Federal Communications Commission because he is transmitting radio signals. The Commission has taken the position that it can issue a license with restrictions and conditions as to what the microwave operator can transmit, even though section 326 of the Communications Act prohibits censorship.

If the Congress passes H.R. 13286 it will open the door wide for the Federal Communications Commission to gain jurisdiction over the reception of television and radio signals—jurisdiction positively denied the Federal Communications Commission under the Communications Act as amended in 1934. It will enable the Commission to determine what can be received by the viewers of this Nation from satellite transmittals, as well as local broadcasting stations and network broadcasts. Freedom requires

that full freedom of communications and information be preserved and protected. The passage of H.R. 13286 would do irreparable damage to this freedom. The people in the fringe areas of radio and television reception would be at the mercy of the Federal Communications Commission and its rulemaking powers.

* * *

It is to be noted that the Federal Communications Commission, although previously denying jurisdiction in the field of CATV, in the early months of 1966 completely reversed their position and assumed jurisdiction over all CATV operations. Lawsuits were filed and are now pending. The Federal Communications Commission, no doubt fearing that it had flagrantly overstepped its jurisdiction, came to the Congress to put its stamp of approval on such action. It is asking the Congress at the present time to give it unbridled authority to control every aspect of the CATV business, a power it has never had over the broadcasting business, but which it wants badly—an entirely new concept in governmental regulation.

The Congress of the United States should not abdicate its legislative powers and delegate to a commission the power to write substantive law by rules and regulations promulgated by an appointed body.

If the Federal Government is to enter a new field of regulation, the manner and extent to which this will be undertaken should be definitely and explicitly spelled out by the duly elected representatives of the people of this country in the Congress of the United States and not by a board, a bureau, or a commission wholly and completely insulated from the electorate. (H.R. Rep. No. 1635, pp. 23-29)

The minority views, in respect to the powers of the Commission and its lack of jurisdiction over CATV, were not disputed by the majority, which merely urged passage of the legislation. A second minority report also strenuously objected to the jurisdictional grab by the FCC.

> Community antenna television systems have been around since 1950, and until 1965 the Federal Communications Commission very clearly indicated that it did not pretend to have jurisdiction over the transmission of broadcast signals by cable. In fact it specifically denied having such jurisdiction. Suddenly, however, the Commission did a complete turnabout and argued that it had always possessed authority to regulate cable television as an extension of broadcasting and its recognized interstate character. By a 5 to 2 decision the Commission determined that the Communications Act of 1934 meant something else and something more than it clearly is. When we consider the fact that the makeup of this Federal agency changes rapidly, such action can lead to dangerous consequences.
>
> Apparently uncertain of its ground, the Commission prepared and suggested a most peculiar piece of legislation which is H.R. 13286. Even a casual reading of this bill will indicate that it makes no attempt to determine a broad policy under which the CATV industry should develop in conjunction with the broadcasting industry. Instead it merely grants broad authority, throwing the whole problem to the Federal Communications Commission and hoping for the best.
>
> Most of the 30 amendments which were offered by members of the committee during the deliberations on this bill were intended to show the will of

Congress and to provide reasonably clear guidelines. They were offered in an attempt to make this bill at least reasonably consistent with past principles for the regulation of industry. They were defeated.

The result of passing H.R. 13286 would be to create havoc within an industry of great importance to the public because the policies adopted by the Commission for its regulation today could well be reversed or radically changed a month or a year hence. There are no general principles to which the industry can point or by which the Congress may oversee the activities of its creature, the Federal Communications Commission.

In the case of broadcasting facilities the Federal Communications Commission must allocate a frequency and issue a license therefor. In the case of community antenna systems there is no provision for licensing, but the bill does grant authority to issue permits for construction. This of course means that construction authority can be denied to any applicant. Under the terms of this bill construction permits would be within the complete discretion of the Commission. In our opinion this grants to the Federal Communications Commission a completely unacceptable and probably unconstitutional power over this industry.

* * *

There are presently pending lawsuits which will determine whether or not the Federal Communications Commission was right when it first denied having jurisdiction over CATV or whether it was right later when it reversed itself. Also pending are lawsuits to determine the applicability of the copyright laws to material carried by CATV systems.

> The determination of these matters requires no legislation and little purpose is served in passing such legislation at this time, particularly since it does not purport to lay down realistic policies and guidelines within which regulation of the CATV industry can logically proceed. (H.R. No. 1635, pp. 26-27)

The bill failed to reach the floor for vote.

APPENDIX C

Statutes and Administrative Rules
Administrative Procedure Act, 5 U.S.C.
Sections:

Section 551 - Definitions

(4) "rule" means the whole or a part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the organization, procedure, or practice requirements of an agency and includes the approval or prescription for the future of rates, wages, corporate or financial structures or reorganizations thereof, prices, facilities, appliances, services or allowances therefor or of valuations, costs, or accounting, or practices bearing on any of the foregoing;

(5) "rule making" means agency process for formulating, amending, or repealing a rule;

(6) "order" means the whole or a part of a final disposition, whether affirmative, negative, injunctive, or declaratory in form, of an agency in a matter other than rule making but including licensing;

(7) "adjudication" means agency process for the formulation of an order;

(8) "license" includes the whole or a part of an agency permit, certificate, approval, registration, charter, membership, statutory exemption or other form of permission;

(9) "licensing" includes agency process respecting the grant, renewal, denial, revocation, suspension, annulment, withdrawal, limitation, amendment, modification, or conditioning of a license;

(10) "sanction" includes the whole or a part of an agency—

(A) prohibition, requirement, limitation, or other condition affecting the freedom of a person;

(B) withholding of relief;

(C) imposition of penalty or fine;

(D) destruction, taking, seizure, or withholding of property;

(E) assessment of damages, reimbursement, restitution, compensation, costs, charges, or fees;

Section 551 (Cont.)

(F) requirement, revocation, or suspension of a license; or

(G) taking other compulsory or restrictive action;

(11) "relief" includes the whole or a part of an agency—

(A) grant of money, assistance, license, authority, exemption, exception, privilege, or remedy;

(B) recognition of a claim, right, immunity, privilege, exemption, or exception; or

(C) taking of other action on the application or petition of, and beneficial to, a person;

Section 554 - Adjudications

(a) This section applies, according to the provisions thereof, in every case of adjudication required by statute to be determined on the record after opportunity for an agency hearing, except to the extent that there is involved—

(1) a matter subject to a subsequent trial of the law and the facts de novo in a court;

(2) the selection or tenure of an employee, except a hearing examiner appointed under section 3105 of this title;

(3) proceedings in which decisions rest solely on inspections, tests, or elections;

(4) the conduct of military or foreign affairs functions;

(5) cases in which an agency is acting as an agent for a court; or

(6) the certification of worker representatives.

(b) Persons entitled to notice of an agency hearing shall be timely informed of—

(1) the time, place, and nature of the hearing;

(2) the legal authority and jurisdiction under which the hearing is to be held; and

(3) the matters of fact and law asserted.

When private persons are the moving parties, other parties to the proceeding shall give prompt notice of issues controverted in fact or law; and in other instances agencies may by rule require responsive pleading. In fixing the time and place for hearings, due regard shall be had for the convenience and necessity of the parties or their representatives.

(c) The agency shall give all interested parties opportunity for—

(1) the submission and consideration of facts, arguments, offers of settlement, or proposals of adjustment when time, the nature of the proceeding, and the public interest permit; and

(2) to the extent that the parties are unable so to determine a controversy by consent, hearing and decision on notice and in accordance with sections 556 and 557 of this title.

(d) The employee who presides at the reception of evidence pursuant to section 556 of this title shall make the recommended decision or initial decision required by section 557 of this title, unless he becomes unavailable to the agency. Except to the extent required for the disposition of ex parte matters as authorized by law, such an employee may not—

(1) consult a person or party on a fact in issue, unless on notice and opportunity for all parties to participate; or

(2) be responsible to or subject to the supervision or direction of an employee or agent engaged in the performance of investigative or prosecuting functions for an agency.

An employee or agent engaged in the performance of investigative or prosecuting functions for an agency in a case may not, in that or a factually related case, participate or advise in the decision, recommended decision, or agency review pursuant to section 557 of this title, except as witness or counsel in public proceedings. This subsection does not apply—

(A) in determining applications for initial licenses;

(B) to proceedings involving the validity or application of rates, facilities, or practices of public utilities or carriers; or

(C) to the agency or a member or members of the body comprising the agency.

(e) The agency, with like effect as in the case of other orders, and in its sound discretion, may issue a declaratory order to terminate a controversy or remove uncertainty.

Section 556 - Hearings; presiding employees; powers and duties; burden of proof; evidence: record as basis of decision

(a) This section applies, according to the provisions thereof, to hearings required by section 553 or 554 of this title to be conducted in accordance with this section.

(b) There shall preside at the taking of evidence—

(1) the agency;

(2) one or more members of the body which comprises the agency; or

(3) one or more hearing examiners appointed under section 3105 of this title.

This subchapter does not supersede the conduct of specified classes of proceedings, in whole or in part, by or before boards or other employees specially provided for by or designated under statute. The functions of presiding employees and of employees participating in decisions in accordance with section 557 of this title shall be conducted in an impartial manner. A presiding or participating employee may at any time disqualify himself. On the filing in good faith of a timely and sufficient affidavit of personal bias or other disqualification of a presiding or participating employee, the agency shall determine the matter as a part of the record and decision in the case.

(c) Subject to published rules of the agency and within its powers, employees presiding at hearings may—

(1) administer oaths and affirmations;

(2) issue subpenas authorized by law;

(3) rule on offers of proof and receive relevant evidence;

(4) take depositions or have depositions taken when the ends of justice would be served;

(5) regulate the course of the hearing;

(6) hold conferences for the settlement or simplication of the issues by consent of the parties;

(7) dispose of procedural requests or similar matters;

(8) make or recommend decisions in accordance with section 557 of this title; and

(9) take other action authorized by agency rule consistent with this subchapter.

Section 556 (Cont.)

(d) Except as otherwise provided by statute, the proponent of a rule or order has the burden of proof. Any oral or documentary evidence may be received, but the agency as a matter of policy shall provide for the exclusion of irrelevant, immaterial, or unduly repetitious evidence. A sanction may not be imposed or rule or order issued except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable, probative, and substantial evidence. A party is entitled to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts. In rule making or determining claims for money or benefits or applications for initial licenses an agency may, when a party will not be prejudiced thereby, adopt procedures for the submission of all or part of the evidence in written form.

(e) The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, constitutes the exclusive record for decision in accordance with section 557 of this title and, on payment of lawfully prescribed costs, shall be made available to the parties. When an agency decision rests on official notice of a material fact not appearing in the evidence in the record, a party is entitled, on timely request, to an opportunity to show the contrary.

Section 557 - Initial decisions; conclusiveness; review by agency; submissions by parties; contents of decisions; record

(a) This section applies, according to the provisions thereof, when a hearing is required to be conducted in accordance with section 556 of this title.

(b) When the agency did not preside at the reception of the evidence, the presiding employee or, in cases not subject to section 554 (d) of this title, an employee qualified to preside at hearings pursuant to section 556 of this title, shall initially decide the case unless the agency requires, either in specific cases or by general rule, the entire record to be certified to it for decision. When the presiding employee makes an initial decision, that decision then becomes the decision of the agency without further proceedings unless there is an appeal to, or review on motion of, the agency within time provided by

Section 557 (Cont.)

rule. On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule. When the agency makes the decision without having presided at the reception of the evidence, the presiding employee or an employee qualified to preside at hearings pursuant to section 556 of this title shall first recommend a decision, except that in rule making or determining applications for initial licenses—

(1) instead thereof the agency may issue a tentative decision or one of its responsible employees may recommend a decision; or

(2) this procedure may be omitted in a case in which the agency finds on the record that due and timely execution of its functions imperatively and unavoidably so requires.

(c) Before a recommended, initial, or tentative decision, or a decision on agency review of the decision of subordinate employees, the parties are entitled to a reasonable opportunity to submit for the consideration of the employees participating in the decisions—

(1) proposed findings and conclusions; or

(2) exceptions to the decisions or recommended decisions of subordinate employees or to tentative agency decisions; and

(3) supporting reasons for the exceptions or proposed findings or conclusions.

The record shall show the ruling on each finding, conclusion, or exception presented. All decisions, including initial, recommended, and tentative decisions, are a part of the record and shall include a statement of—

(A) findings and conclusions, and the reasons or basis therefor, on all the material issues of fact, law, or discretion presented on the record; and

(B) the appropriate rule, order, sanction, relief, or denial thereof.

Section 558 - Imposition of sanctions; determination of applications for licenses; suspension, revocation, and expiration of licenses

(a) This section applies, according to the provisions thereof, to the exercise of a power or authority.

Section 558 - (Cont.)

(b) A sanction may not be imposed or a substantive rule or order issued except within jurisdiction delegated to the agency and as authorized by law.

(c) When application is made for a license required by law, the agency, with due regard for the rights and privileges of all the interested parties or adversely affected persons and within a reasonable time, shall set and complete proceedings required to be conducted in accordance with sections 556 and 557 of this title or other proceedings required by law and shall make its decision. Except in cases of willfulness or those in which public health, interest, or safety requires otherwise, the withdrawal, suspension, revocation, or annulment of a license is lawful only if, before the institution of agency proceedings therefor, the licensee has been given—

(1) notice by the agency in writing of the facts or conduct which may warrant the action; and

(2) opportunity to demonstrate or achieve compliance with all lawful requirements.

When the licensee has made timely and sufficient application for a renewal or a new license in accordance with agency rules, a license with reference to an activity of a continuing nature does not expire until the application has been finally determined by the agency.

Communications Act of 1934, 47 U.S.C. Sections:
Section 151 - Purposes of act; Creation of Federal Communications Commission

For the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, for the purpose of promoting safety of life and property through the use of wire and radio communication,[1] and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication, there is hereby created a commission to be known as the "Federal Communications Commission," which shall be constituted as hereinafter provided, and which shall execute and enforce the provisions of this Act.

Section 154 - Provisions relating to the Commission

(i) The Commission may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this Act, as may be necessary in the execution of its functions.

Section 303 - General powers of the Commission

(f) Make such regulations not inconsistent with law as it may deem necessary to prevent interference between stations and to carry out the provisions of this Act: *Provided, however*, that changes in the frequencies, authorized power, or in the times of operation of any station, shall not be made without the consent of the station licensee unless, after a public hearing, the Commission shall determine that such changes will promote public convenience or interest or will serve public necessity, or the provisions of this Act will be more fully complied with;

(h) Have authority to establish areas or zones to be served by any station;

(m)(2) No order of suspension of any operator's license shall take effect until fifteen days' notice in writing thereof, stating the cause for the proposed suspension, has been given to the operator licensee who may make written application to the Commission at any time within said fifteen days for a hearing upon such order. The notice to the operator licensee shall not be effective until actually received by him, and from that time he shall have fifteen days in which to mail the said application. In the event that physical conditions prevent mailing of the application at the expiration of the fifteen-day period, the application shall then be mailed as soon as possible thereafter, accompanied by a satisfactory explanation of the delay. Upon receipt by the Commission of such application for hearing, said order of suspension shall be held in abeyance until the conclusion of the hearing which shall be conducted under such rules as the Commission may prescribe. Upon the conclusion of said hearing the Commission may affirm, modify, or revoke said order of suspension.

Section 303 (Cont.)

(p) Have authority to cause to be published such call letters and such other announcements and data as in the judgment of the Commission may be required for the efficient operation of radio stations subject to the jurisdiction of the United States and for the proper enforcement of this Act:

(r) Make such rules and regulations and prescribe such restrictions and conditions, not inconsistent with law, as may be necessary to carry out the provisions of this Act, or any international radio or wire communications treaty or convention, or regulations annexed thereto, including any treaty or convention insofar as it relates to the use of radio, to which the United States is or may hereafter become a party.[45]

Section 307 - Allocation of facilities; term of licenses

(b)[46] In considering applications for licenses, and modifications and renewals thereof, when and insofar as there is demand for the same, the Commission shall make such distribution of licenses, frequencies, hours of operation, and of power among the several States and communities as to provide a fair, efficient, and equitable distribution of radio service to each of the same.

Section 309 - Action upon applications; form of and conditions attached to licenses

(a) Subject to the provisions of this section, the Commission shall determine, in the case of each application filed with it to which section 308 applies, whether the public interest, convenience, and necessity will be served by the granting of such application, and, if the Commission, upon examination of such application and upon consideration of such other matters as the Commission may officially notice, shall find that public interest, convenience, and necessity would be served by the granting thereof, it shall grant such application.

Section 309 (Cont.)

(e) If, in the case of any application to which subsection (a) of this section applies, a substantial and material question of fact is presented or the Commission for any reason is unable to make the finding specified in such subsection, it shall formally designate the application for hearing on the ground or reasons then obtaining and shall forthwith notify the applicant and all other known parties in interest of such action and the grounds and reasons therefor, specifying with particularity the matters and things in issue but not including issues or requirements phrased generally. When the Commission has so designated an application for hearing, the parties in interest, if any, who are not notified by the Commission of such action may acquire the status of a party to the proceeding thereon by filing a petition for intervention showing the basis for their interest not more than thirty days after publication of the hearing issues or any substantial amendment thereto in the Federal Register.[54b] Any hearing subsequently held upon such application shall be a full hearing in which the applicant and all other parties in interest shall be permitted to participate. The burden of proceeding with the introduction of evidence and the burden of proof shall be upon the applicant, except that with respect to any issue presented by a petition to deny or a petition to enlarge the issues, such burdens shall be as determined by the Commission.

Section 312 - Administrative Sanctions

(a) The Commission may revoke any station license or construction permit—

(1) for false statements knowingly made either in the application or in any statement of fact which may be required pursuant to section 308;

(2) because of conditions coming to the attention of the Commission which would warrant it in refusing to grant a license or permit on an original application;

(3) for willful or repeated failure to operate substantially as set forth in the license;

(4) for willful or repeated violation of, or willful or repeated failure to observe any provision of this Act or any rule or regulation of the Commission authorized by this Act or by a treaty ratified by the United States;

(5) for violation of or failure to observe any final cease and desist order issued by the Commission under this section; or

Section 312 (Cont.)

(6) for violation of section 1304, 1343, or 1464 of title 18 of the United States Code.

(b) Where any person (1) has failed to operate substantially as set forth in a license, (2) has violated or failed to observe any of the provisions of this Act, or section 1304, 1343, or 1464 of title 18 of the United States Code, or (3) has violated or failed to observe any rule or regulation of the Commission authorized by this Act or by a treaty ratified by the United States, the Commission may order such person to cease and desist from such action.

(c) Before revoking a license or permit pursuant to subsection (a), or issuing a cease and desist order pursuant to subsection (b), the Commission shall serve upon the licensee, permittee, or person involved an order to show cause why an order of revocation or a cease and desist order should not be issued. Any such order to show cause shall contain a statement of the matters with respect to which the Commission is inquiring and shall call upon said licensee, permittee, or person to appear before the Commission at a time and place stated in the order, but in no event less than thirty days after the receipt of such order, and give evidence upon the matter specified therein; except that where safety of life or property is involved, the Commission may provide in the order for a shorter period. If after hearing, or a waiver thereof, the Commission determines that an order of revocation or a cease and desist order should issue, it shall issue such order, which shall include a statement of the findings of the Commission and the grounds and reasons therefor and specify the effective date of the order, and shall cause the same to be served on said licensee, permittee, or person.

(d) In any case where a hearing is conducted pursuant to the provisions of this section, both the burden of proceeding with the introduction of evidence and the burden of proof shall be upon the Commission.

(e) The provisions of section 9(b) of the Administrative Procedure Act which apply with respect to the institution of any proceeding for the revocation of a license or permit shall apply also with respect to the institution, under this section, of any proceeding for the issuance of a cease and desist order.[59]

Section 315 - Facilities for candidates for public office

(a) If any licensee shall permit any person who is a legally qualified candidate for any public office to use a broadcasting station, he

Section 315 (Cont.)

shall afford equal opportunities to all other such candidates for tha office in the use of such broadcasting station: *Provided*, That such licensee shall have no power of censorship over the material broadcast under the provisions of this section. No obligation is hereby[61] imposed upon any licensee to allow the use of its station by any such candidate. Appearance by a legally qualified candidate on any—

(1) bona fide newscast,

(2) bona fide news interview,

(3) bona fide news documentary (if the appearance of the candidate is incidental to the presentation of the subject or subjects covered by the news documentary), or

(4) on-the-spot coverage of bona fide news events (including but not limited to political conventions and activities incidental thereto),

shall not be deemed to be use of a broadcasting station within the meaning of this subsection. Nothing in the foregoing sentence shall be construed as relieving broadcasters, in connection with the presentation of newscasts, news interviews, news documentaries, and on-the-spot coverage of news events, from the obligation imposed upon them under this Act[61a] to operate in the public interest and to afford reasonable opportunity for the discussion of conflicting views on issues of public importance.

(b) The charges made for the use of any broadcasting station for any of the purposes set forth in this section shall not exceed the charges made for comparable use of such station for other purposes.

(c) The Commission shall prescribe appropriate rules and regulations to carry out the provisions of this section.[61b]

Section 316 - Modification by Commission of construction permits or licenses

(a) Any station license or construction permit may be modified by the Commission either for a limited time or for the duration of the term thereof, if in the judgment of the Commission such action will promote the public interest, convenience, and necessity, or the provisions of this Act or of any treaty ratified by the United States will be more fully complied with. No such order of modification shall become final until the holder of the license or permit shall have been notified in writing of the proposed action and the grounds and reasons therefor, and shall have been given reasonable opportunity, in no event less than thirty days, to show cause by public hearing, if requested,

Section 316 (Cont.)

why such order of modification should not issue: *Provided*, That where safety of life or property is involved, the Commission may by order provide for a shorter period of notice.

(b) In any case where a hearing is conducted pursuant to the provisions of this section, both the burden of proceeding with the introduction of evidence and the burden of proof shall be upon the Commission.[62]

Section 317 - Announcement with respect to certain matter broadcast

(a)(1) All matter broadcast by any radio station for which any money, service or other valuable consideration is directly or indirectly paid, or promised to or charged or accepted by, the station so broadcasting, from any person, shall, at the time the same is so broadcast, be announced as paid for or furnished, as the case may be, by such person: *Provided*, That "service or other valuable consideration" shall not include any service or property furnished without charge or at a nominal charge for use on, or in connection with, a broadcast unless it is so furnished in consideration for an identification in a broadcast of any person, product, service, trademark, or brand name beyond an identification which is reasonably related to the use of such service or property on the broadcast.

(2) Nothing in this section shall preclude the Commission from requiring that an appropriate announcement shall be made at the time of the broadcast in the case of any political program or any program involving the discussion of any controversial issue for which any films, records, transcriptions, talent, scripts, or other material or service of any kind have been furnished, without charge or at a nominal charge, directly or indirectly, as an inducement to the broadcast of such program.

(b) In any case where a report has been made to a radio station, as required by section 508 of this Act, of circumstances which would have required an announcement under this section had the consideration been received by such radio station, an appropriate announcement shall be made by such radio station.

(c) The licensee of each radio station shall exercise reasonable diligence to obtain from its employees, and from other persons with whom it deals directly in connection with any program or program matter for broadcast, information to enable such licensee to make the announcement required by this section.

Section 317 (Cont.)

(d) The Commission may waive the requirement of an announcement as provided in this section in any case or class of cases with respect to which it determines that the public interest, convenience, or necessity does not require the broadcasting of such announcement.

(e) The Commission shall prescribe appropriate rules and regulations to carry out the provisions of this section.[63]

Section 326 - Censorship; indecent language

Nothing in this Act shall be understood or construed to give the Commission the power of censorship over the radio communications or signals transmitted by any radio station, and no regulation or condition shall be promulgated or fixed by the Commission which shall interfere with the right of free speech by means of radio communication.[71]

Section 403 - Inquiry by Commission on its own motion

The Commission shall have full authority and power at any time to institute an inquiry, on its own motion, in any case and as to any matter or thing concerning which complaint is authorized to be made, to or before the Commission by any provision of this Act, or concerning which any question may arise under any of the provisions of this Act, or relating to the enforcement of any of the provisions of this Act. The Commission shall have the same powers and authority to proceed with any inquiry instituted on its own motion as though it had been appealed to by complaint or petition under any of the provisions of this Act, including the power to make and enforce any order or orders in the case, or relating to the matter or thing concerning which the inquiry is had, excepting orders for the payment of money.

Section 508 - Disclosure of certain payments

(a) Subject to subsection (d), any employee of a radio station who accepts or agrees to accept from any person (other than such station), or any person (other than such station) who pays or agrees to pay such employee, any money, service or other valuable consideration for the broadcast of any matter over such station shall, in advance of such broadcast, disclose the fact of such acceptance or agreement to such station.

(b) Subject to subsection (d), any person who, in connection with the production or preparation of any program or program matter which is intended for broadcasting over any radio station, accepts or agrees to accept, or pays or agrees to pay, any money, service or other valuable consideration for the inclusion of any matter as a part of such program or program matter, shall, in advance of such broadcast, disclose the fact of such acceptance or payment or agreement to the payee's employer, or to the person for whom such program or program matter is being produced, or to the licensee of such station over which such program is broadcast.

(c) Subject to subsection (d), any person who supplies to any other person any program or program matter which is intended for broadcasting over any radio station shall, in advance of such broadcast, disclose to such other person any information of which he has knowledge, or which has been disclosed to him, as to any money, service or other valuable consideration which any person has paid or accepted, or has agreed to pay or accept, for the inclusion of any matter as a part of such program or program matter.

(d) The provisions of this section requiring the disclosure of information shall not apply in any case where, because of a waiver made by the Commission under section 317(d), an announcement is not required to be made under section 317.

(e) The inclusion in the program of the announcement required by section 317 shall constitute the disclosure required by this section.

(f) The term "service or other valuable consideration" as used in this section shall not include any service or property furnished without charge or at a nominal charge for use on, or in connection with, a broadcast, or for use on a program which is intended for broadcasting over any radio station, unless it is so furnished in consideration for an identification in such broadcast or in such program of any person, product, service, trademark, or brand name beyond an identification which is reasonably related to the use of such service or property in such broadcast or such program.

(g) Any person who violates any provision of this section shall, for each such violation, be fined not more than $10,000 or imprisoned not more than one year, or both.[102]

Selected provisions of the Federal Communications Commission's Microwave and CATV rules and regulations, 47 C.F.R. Sections

§ 21.712 Authorizations for fixed stations to relay television signals to CATV systems.

Authorizations (including initial grants, modifications, assignments or transfers of control, and renewals) in this service to establish or operate fixed stations used to relay television signals to community antenna television systems (CATV systems), either directly or indirectly, shall contain the condition that the licensee carrier shall offer service by means of such stations in accordance with the following requirements, which the licensee carrier shall also include, or cause to be included, in its tariffs for service to any CATV system or other subscriber proposing to utilize such service to relay television signals to any CATV system, either directly or indirectly:

(a) *Certification.* The carrier shall require that any subscriber ordering service indicate whether the service is to be utilized for relaying television signals to any CATV system, either directly or indirectly, and in such event the carrier shall require that the subscriber at least thirty (30) days prior to receiving service file a certification with the carrier, and a copy for the Federal Communications Commission, stating that he has complied with the notification provisions set forth in paragraph (b) of this section, and that each such CATV system will comply with the provisions set forth in paragraphs (c) through (i) of this section. Such certification to the carrier and copy for the Federal Communications Commission shall be supported by copies of the letters of notification sent to television broadcast licensees or permittees pursuant to the requirements of § 21.712(b), and by a statement from each such CATV system indicating willingness to comply with § 21.712. Such copies for the Federal Communications Commission shall be forwarded to the Commission by the carrier at least thirty (30) days prior to commencing service.

(b) *Notification of request for service.* Any such CATV system or other subscriber proposing to utilize

such service to relay television signals to any CATV system, either directly or indirectly, shall notify the licensee or permittee of any television broadcast station, within whose predicted Grade B contour the CATV system operates or will operate in whole or in part, and the licensee or permittee of any 100 watts or higher power translator station operating in the community of the system, of the request for service. Where it is proposed to extend the signal of any noncommercial educational television station beyond its Grade B contour into a community with an unoccupied reserved educational television channel assignment under § 73.606 of this chapter, the notice shall also be served upon the superintendents of schools in the community and county and the local, area, and State educational television agencies, if any. Such notice shall include the fact of the request for service, identification of each CATV system to utilize the service requested (either directly or indirectly), identification of the community served or to be served by each CATV system, and the television station(s) whose programs will be distributed by each such CATV system.

(c) *Stations required to be carried.* Within the limits of its channel capacity, any such CATV system shall carry the signals of operating or subsequently authorized and operating television broadcast and 100 watts or higher power translator stations in the following order of priority, upon the request of the licensee or permittee of the relevant station:

(1) First, all commercial and noncommercial educational stations within whose principal community contours the system or the community of the system is located, in whole or in part;

(2) Second, all commercial and noncommercial educational stations within whose Grade A contours the system or the community of the system is located, in whole or in part;

(3) Third, all commercial and noncommercial educational stations within whose Grade B contours the system or the community of the system is located, in whole or in part; and

(4) Fourth, all commercial and noncommercial educational translator stations operating in the community

of the system, in whole or in part, with 100 watts or higher power.

(d) *Exceptions.* Nothwithstanding the requirements of paragraph (c) of this section,

(1) The system need not carry the signal of any station, if (i) that station's network programming is substantially duplicated by one or more stations of higher priority and (ii) carrying it would, because of limited channel capacity, prevent the system from carrying the signal of an independent commercial station or a noncommercial educational station.

(2) In cases where (i) there are two or more signals of equal priority which substantially duplicate each other, and (ii) carrying all such signals would, because of limited channel capacity, prevent the system from carrying the signal of an independent commercial station or a noncommercial educational station, the system need not carry all such substantially duplicating signals, but may select among them to the extent necessary to preserve its ability to carry the signals of independent commercial or noncommercial educational stations.

(3) The system need not carry the signal of any television translator station if: (i) The system is carrying the signal of the originating station, or (ii) the system is within the Grade B or higher priority contour of a station carried on the system whose programing is substantially duplicated by the translator; *Provided, however,* That where the originating station is carried in place of the translator station, the priority for purposes of paragraph (g) of this section shall be that of the translator station unless the priority of the originating station is higher.

(4) In the event that the system operates, or its community is located, within the Grade B or higher priority contours of both a satellite station and its parent station, the system need carry only the station with the higher priority; if the satellite station and its parent station are of equal priority, the system may select between them.

[§ *21.712(c) and (d)(3) amended, (d)(4) adopted eff. 2-28-67; VII (66)-3*]

(e) *Special requirements in the event of noncarriage.* Where the system does not carry the signals of one or more stations within whose Grade B or higher priority contour it operates, or the signals of one or more 100 watts or higher power translator stations located in its community, the system shall offer and maintain, for each subscriber, an adequate switching device to allow the subscriber to choose between cable and noncable reception, unless the subscriber affirmatively indicates in writing that he does not desire this device.

(f) *Manner of carriage.* Where the signal of any station is required to be carried under this section,

(1) The signal shall be carried without material degradation in quality (within the limitations imposed by the technical state of the art);

(2) The signal shall, upon request of the station licensee or permittee, be carried on the system on the channel on which the station is transmitting (where practicable without material degradation); and

(3) The signal shall, upon the request of the station licensee or permittee, be carried on the system on no more than one channel.

(g) *Stations entitled to program exclusivity.* Any such system which operates, in whole or in part, within the Grade B or higher priority contour of any commercial or noncommercial educational television station or within the community of a fourth priority television translator station, and which carries the signal of such station shall, upon request of the station licensee or permittee, maintain the station's exclusivity as a program outlet against lower priority or more distant duplicating signals, but not against signals of equal priority, in the manner and to the extent specified in paragraphs (h) and (i) of this section.

(h) *Program exclusivity; extent of protection.* Where a station is entitled to program exclusivity, the CATV system shall, upon request of the station licensee or permittee, refrain from duplicating any program broadcast by such station on the same day as its broadcast by the station, if the CATV operator has received notification from the requesting station of the date and time of its broadcast of the program and the date and time of any broadcast to be deleted, as

soon as possible and in any event no later than 48 hours prior to the broadcast to be deleted. Upon request of the CATV system, such notice shall be given at least 8 days prior to the date of any broadcast to be deleted.

(i) *Exceptions.* Notwithstanding the requirements of paragraph (h) of this section.

(1) The CATV system need not delete reception of a network program if, in so doing, it would leave available for reception by subscribers, at any time, less than two network programs (including those broadcast by any stations whose signals are being carried and whose program exclusivity is being protected pursuant to the requirements of this section);

(2) The system need not delete reception of a network program which is scheduled by the network between the hours of 6 and 11 p.m., eastern time, but is broadcast by the station requesting deletion, in whole or in part, outside of the period which would normally be considered prime time for network programming in the time zone involved; and

(3) The system need not delete reception of any program consisting of the broadcast coverage of a speech or other event as to which the time of presentation is of special significance, except where the program is being simultaneously broadcast by a station entitled to program exclusivity.

(4) The system need not delete reception of any program which would be carried on the system in color but will be broadcast in black and white by the station requesting deletion.

(j) *Disputes between television broadcast or translator stations and CATV systems; requests for waiver of the rules or for different treatment.* In the event that a dispute should arise, at any time, between a television broadcast or translator station and a CATV system served under an authorization subject to this section, on the question of whether the CATV system is complying with the applicable requirements, the matter may be referred to the Commission for a ruling pursuant to the provisions of § 74.1109 of this chapter, either by the licensee carrier, or by the station, or

CATV system, with notice to the licensee carrier. Where a dispute has been referred to the Commission for a ruling or where a petition for waiver of the rules or for different requirements has been filed under § 74.1109 of this chapter, with notice to the licensee carrier, microwave service to the relevant subscriber shall not be commenced or terminated until thirty (30) days after the Commission's ruling has been received by the licensee carrier.

(k) *Interim requirement.* No CATV system shall be provided with microwave service, either directly or indirectly, if the operation of such CATV system would be inconsistent with § 74.1107 of this chapter.

Note 1: As used in § 21.712(b), the term "predicted Grade B contour" means the field intensity contour defined in § 73.683(a) of this chapter, the location of which is determined exclusively by means of the calculations prescribed in § 73.684 of this chapter.

SUBPART K—COMMUNITY ANTENNA TELEVISION SYSTEMS

[*Subpart K (§§ 74.1101–74.1109) as adopted eff. 4–18–66; except for § 74.1103 which is eff. 6–17–66 as it pertains to existing operations of nonmicrowave CATV systems and §§ 74.1105, 74.1107, and 74.1109 which are eff. 3–17–66; III(64)–12*]

§ 74.1100 Cross reference.

See § 74.11.

[*§ 74.1100 adopted eff. 2–28–67; III(64)–16*]

§ 74.1101 Definitions.

(a) *Community antenna television system.* The term "community antenna television system" ("CATV system") means any facility which, in whole or in part, receives directly or indirectly over the air and amplifies or otherwise modifies the signals transmitting programs broadcast by one or more television stations and distributes such signals by wire or cable to subscribing members of the public who pay for such service, but such term shall not include (1) any such facility which serves fewer than 50 subscribers, or (2) any such facility which serves only the residents of one or more apartment dwellings under common ownership, control, or management, and commercial establishments located on the premises of such an apartment house.

(b) *Television station; television broadcast station; television translator station.* The terms "television station" and "television broadcast station" mean any television broadcasting station operating on a channel regularly assigned to its community by § 73.606 of this chapter. The term "television translator station" means a television broadcast translator station as defined in § 74.701 of this chapter. A television translator station which is licensed to and rebroadcasts the programing of a television broadcast station within that station's Grade B contour, shall be deemed an extension of the originating station.

(c) *Principal community contour.* The term "principal community contour" means the signal contour which a television station is required to place over its entire principal community by § 73.685(a) of this chapter.

(d) *Grade A and Grade B contours.* The terms "Grade A contour" and "Grade B contour" mean the field intensity contours defined in § 73.683(a) of this chapter.

(e) *Network programing.* The term "network programing" means the programing supplied by a national television network organization.

(f) *Substantially duplicated.* The term "substantially duplicated" means regularly duplicated by the network programing of one or more stations, singly or collectively, in a normal week during the hours of 6 to 11 p.m., local time, for a total of 14 or more hours.

(g) *Priority.* The term "priority" means the priority among stations established in § 74.1103(a).

(h) *Independent station.* The term "independent station" means a television station which is not affiliated with any national television network organization.

(i) *Distant signal.* The term "distant signal" means the signal of a television broadcast station which is extended or received beyond the Grade B contour of that station.

§ 74.1103 Requirement relating to distribution of television signals by community antenna television systems.

No community antenna television system shall supply to its subscribers signals broadcast by one or more television stations, except in accordance with the following conditions:

(a) *Stations required to be carried.* Within the limits of its channel capacity, any such CATV system shall carry the signals of operating or subsequently authorized and operating television broadcast and 100 watts or higher power translator stations in the following order of priority, upon the request of the licensee or permittee of the relevant station:

(1) First, all commercial and noncommercial educational stations within whose principal community contours the system or the community of the system is located, in whole or in part;

(2) Second, all commercial and noncommercial educational stations within whose Grade A contours the system or the community of the system is located, in whole or in part;

(3) Third, all commercial and noncommercial educational stations within whose Grade B contours the system or the community of the system is located, in whole or in part; and

(4) Fourth, all commercial and noncommercial educational translator stations operating in the community of the system, in whole or in part, with 100 watts or higher power.

(b) *Exceptions.* Nothwithstanding the requirements of paragraph (a) of this section,

(1) The system need not carry the signal of any station, if (i) that station's network programing is substantially duplicated by one or more stations of higher priority, and (ii) carrying it would, because of limited channel capacity, prevent the system from carrying the signal of an independent commercial station or a noncommercial educational station.

(2) In cases where (i) there are two or more signals of equal priority which substantially duplicate each other, and (ii) carrying all such signals would, because of limited channel capacity, prevent the system from carrying the signal of an independent commercial station or a noncommercial educational station, the system need not carry all such substantially duplicating signals, but may select among them to the extent necessary to preserve its ability to carry the signals of independent commercial or noncommercial educational stations.

(3) The system need not carry the signal of any television translator station if: (i) The system is carrying the signal of the originating station, or (ii) the system is within the Grade B or higher priority contour of a station carried on the system whose programing is substantially duplicated by the translator; *Provided, however,* That where the originating station is carried in place of the translator station, the priority for purposes of paragraph (e) of this section shall be that of the translator station unless the priority of the originating station is higher.

(4) In the event that the system operates, or its community is located, within the Grade B or higher priority contours of both a satellite and its parent station, the system need carry only the station with the higher priority, if the satellite station and its parent station are of equal priority, the system may select between them.

(c) *Special requirements in the event of noncarriage.* Where the system does not carry the signals of one or more stations within whose Grade B or higher priority contour it operates, or the signals of one or more 100 watts or higher power translator stations located in its community, the system shall offer and maintain, for each subscriber, an adequate switching device to allow the subscriber to choose between cable and noncable reception, unless the subscriber affirmatively indicates in writing that he does not desire this device.

(d) *Manner of carriage.* Where the signal of any station is required to be carried under this section,

(1) The signal shall be carried without material degradation in quality (within the limitations imposed by the technical state of the art);

(2) The signal shall, upon request of the station licensee or permittee, be carried on the system on the channel on which the station is transmitting (where practicable without material degradation); and

(3) The signal shall, upon the request of the station licensee or permittee, be carried on the system on no more than one channel.

(e) *Stations entitled to program exclusivity.* Any such system which operates, in whole or in part, within the Grade B or higher priority contour of any commercial or noncommercial educational television station or within the community of a fourth priority television translator station, and which carries the signal of such station shall, upon request of the station licensee or permittee, maintain the station's exclusivity as a program outlet against lower priority or more distant duplicating signals, but not against signals of equal priority, in the manner and to the extent specified in paragraphs (f) and (g) of this section.

'(f) *Program exclusivity: extent of protection.* Where a station is entitled to program exclusivity, the CATV system shall, upon the request of the station licensee or permittee, refrain from duplicating any program broadcast by such station, on the same day as its broadcast by the station, if the CATV operator has received notification from the requesting station of the date and time of its broadcast of the program and the date and time of any broadcast to be deleted, as soon as possible and in any event no later than 48 hours prior to the broadcast to be deleted. Upon request of the CATV system, such notice shall be given at least 8 days prior to the date of any broadcast to be deleted. '

(g) *Exceptions.* Notwithstanding the requirements of paragraph (f) of this section.

(1) The CATV system need not delete reception of a network program if, in so doing, it would leave available for reception by subscribers, at any time, less than the programs of two networks (including those broadcast by any stations whose signals are being carried and whose program exclusivity is being protected pursuant to the requirements of this section);

(2) The system need not delete reception of a network program which is scheduled by the network between the hours of 6 and 11 p.m., eastern time, but is broadcast by the station requesting deletion, in whole or in part, outside of the period which would normally be considered prime time for network programing in the time zone involved;

(3) The system need not delete reception of any program consisting of the broadcast coverage of a speech or other event as to which the time of presentation is of special significance, except where the program is being simultaneously broadcast by a station entitled to program exclusivity; and

(4) The system need not delete reception of any program which would be carried on the system in color but will be broadcast in black and white by the station requesting deletion.

[*§ 74.1103(a) and (b)(3) amended, (b)(4) adopted eff. 2-28-67; III(64)-16*]

§ 74.1105 Notification prior to the commencement of new service.

(a) No CATV system shall commence operations in a community or commence supplying to its subscribers the signal of any television broadcast station carried beyond the Grade B contour of the station, unless the system has given prior notice of the proposed new service to the licensee or permittee of any television broadcast station within whose predicted Grade B contour the system operates or will operate, and to the licensee or permittee of any 100 watts or higher power translator station operating in the community of the system, and has furnished a copy of each such notification to the Federal Communications Commission, within

sixty (60) days after obtaining a franchise or entering into a lease or other arrangement to use facilities; in any event, no CATV system shall commence such operations until thirty (30) days after notice has been given. Such notice shall be given by existing systems which propose to add new distant signals at least thirty (30) days prior to commencing service and by systems which propose to extend lines into another community within sixty (60) days after obtaining a franchise or entering into a lease or other arrangement to use facilities or where no new local authorization or contractual arrangement is necessary, at least thirty (30) days prior to commencing service. Where it is proposed to extend the signal of any noncommercial educational television station beyond its Grade B contour into a community with an unoccupied reserved educational television channel assignment under § 73.606 of this chapter, the notice shall also be served upon the superintendents of schools in the community and county in which the system will operate and the local, area, and State educational television agencies, if any.

(b) The notice shall include the name and address of the system, identification of the community to be served, the television signals to be distributed, and the estimated time operations will commence.

(c) Where a petition with respect to the proposed service is filed with the Commission, pursuant to § 74.1109 of this chapter, within thirty (30) days after notice, new service which is challenged in the petition shall not be commenced until after the Commission's ruling on the petition or on the interlocutory question of temporary relief pending further procedures; *Provided, however*, That service shall not be commenced in violation of the terms of any specified temporary relief or of the provisions of § 74.1107 of this chapter. Where no petition pursuant to § 74.1109 has been filed within thirty (30) days after notice, service may be commenced at any time thereafter, subject, however, to the provisions of § 74.1107.

(d) The provisions of this section do not apply to any signals which were being supplied to subscribers in the community of the CATV system on March 17, 1966, unless it is proposed to extend lines into another community.

NOTE 1: As used in § 74.1105, the term "predicted Grade B contour" means the field intensity contour defined in § 73.683(a) of this chapter, the location of which is deter-

mined exclusively by means of the calculations prescribed in § 73.684 of this chapter.

NOTE 2: As used in § 74.1105, the term "television broadcast station" includes foreign television broadcast stations.

[*§ 74.1105 amended in III(64)–16; Note 2 adopted eff. 7–14–67; III(64)–18*]

§ 74.1107 Requirement for showing in evidentiary hearing and Commission approval in top 100 television markets; other procedures.

(a) No CATV system operating in a community within the predicted Grade A contour of a television broadcast station in the 100 largest television markets shall extend the signal of a television broadcast station beyond the Grade B contour of that station, except upon a showing approved by the Commission that such extension would be consistent with the public interest, and specifically the establishment and healthy maintenance of television broadcast service in the area. Commission approval of a request to extend a signal in the foregoing circumstances will be granted where the Commission, after consideration of the request and all related materials in a full evidentiary hearing, determines that the requisite showing has been made. The market size shall be determined by the rating of the American Research Bureau, on the basis of the net weekly circulation for the most recent year.

(b) A request under paragraph (a) of this section shall be filed after the CATV system has obtained any necessary franchise for operation or has entered into a lease or other arrangement to use facilities and shall set forth the name of the community involved, the date on which a franchise was obtained, the signal or signals proposed to be extended beyond their Grade B contours, the date on which copies of the notifications required by § 74.1105 of this chapter were filed with the Commission, and the specific reasons why it is urged that such extension is consistent with the public interest. Public notice will be given of the filing of such a request, and interested parties may file a response or statement within thirty (30) days after such public notice. A reply to such a response or statement may be filed within a twenty (20) day period thereafter. The Commission shall designate the request for an evidentiary hearing on issues to be specified, with the burden of proof and the burden of proceeding with the introduction of evidence upon the CATV system

making the request, unless otherwise specified by the Commission as to particular issues.

(c) No CATV system, located so as to fall outside the provisions of paragraph (a) of this section, shall extend the signal of a television broadcast station beyond the Grade B contour of that station, where the Commission, upon its own motion or pursuant to a petition filed under § 74.1109, determines, after appropriate proceedings, that such extension would be inconsistent with the public interest, taking into account particularly the establishment and healthy maintenance of television broadcast service in the area.

(d) The provisions of paragraphs (a) and (b) of this section shall not be applicable to any signals which were being supplied by a CATV system to its subscribers in a community on February 15, 1966, and pursuant to a franchise (where necessary) issued on or before that date: *Provided, however*, That any new franchise or amendment of an existing franchise after February 15, 1966, to operate or extend the operations of the CATV system in the same general area or any extension into another community does come within the provisions of paragraphs (a) and (b) of this section: *And provided further*, That no CATV system located in a community in the 100 largest television markets, which was supplying to its subscribers on February 15, 1966, a signal carried beyond its Grade B contour, shall extend such service to new geographical areas within the same community where the Commission, upon petition filed under § 74.1109 by a television broadcast station or other interested person located in the area and after consideration of the response of the CATV system and appropriate proceedings, determines that the public interest, taking into account the considerations set forth in the Second Report and Order in Docket Nos. 14895, 15233, and 15971, FCC 66–220, paragraphs 113–149, would be served by appropriate conditions limiting the geographical extension of the system to new areas in the community. The Commission may also consider, upon the basis of the pleadings before it, whether temporary relief is called for in the public interest, and, if so, the nature of such relief; no CATV system coming within the foregoing provision shall extend its service to new geographical areas in violation of the terms of the specified temporary relief.

(c) Within 60 days of issuance of a request filed pursuant to paragraph (a) of this section, interested parties seeking simultaneous consideration with such request must file appropriate requests for any other CATV system in the same television market. All requests for CATV systems in a given market timely filed with respect to the first request will be processed and considered simultaneously. Later filed requests for the particular market will be subject to chronological processing and may not be considered in the same proceeding as the earlier requests.

NOTE 1: As used in § 74.1107, the term "television broadcast station" includes foreign television broadcast stations.

[§ *74.1107 amended in III(64)–16 and III(64)–17; Note 1 adopted eff. 7–14–67; III(64)–18*]

§ 74.1109 Procedures applicable to petitions for waiver of the rules, additional or different requirements and rulings on complaints or disputes.

(a) Upon petition by a CATV system, an applicant, permittee, or licensee of a television broadcast, translator, or microwave relay station, or by any other interested person, the Commission may waive any provision of the rules relating to the distribution of television broadcast signals by CATV systems, impose additional or different requirements, or issue a ruling on a complaint or disputed question.

(b) The petition may be submitted informally, by letter, but shall be accompanied by an affidavit of service on any CATV system, station licensee, permittee, applicant, or other interested person who may be directly affected if the relief requested in the petition should be granted.

(c) (1) The petition shall state the relief requested and may contain alternative requests. It shall state fully and precisely all pertinent facts and considerations relied upon to demonstrate the need for the relief requested and to support a determination that a grant of such relief would serve the public interest. Factual allegations shall be supported by affidavit of a person or persons with actual knowledge of the facts, and exhibits shall be verified by the person who prepares them.

(2) A petition for a ruling on a complaint or disputed question shall set forth all steps taken by the parties to resolve the problem, except where the only relief sought is a clarification or interpretation of the rules.

(d) Interested persons may submit comments or opposition to the petition within thirty (30) days after it has been filed. Upon good cause shown in the petition, the Commission may, by letter or telegram to known interested persons, specify a shorter time for such submissions. Comments or oppositions shall be served on petitioner and on all persons listed in petitioner's affidavit of service, and shall contain a detailed full showing, supported by affidavit, of any facts or considerations relied upon.

(e) The petitioner may file a reply to the comments or oppositions within twenty (20) days after their submission, which shall be served upon all persons who have filed pleadings and shall also contain a detailed full showing, supported by affidavit, of any additional facts or considerations relied upon. Upon good cause shown, the Commission may specify a shorter time for the filing of reply comments.

(f) The Commission, after consideration of the pleadings, may determine whether the public interest would be served by the grant, in whole or in part, or denial of the request, or may issue a ruling on the complaint or dispute. The Commission may specify other procedures, such as oral argument, evidentiary hearing, or further written submissions directed to particular aspects, as it deems appropriate. In the event that an evidentiary hearing is required, the Commission will determine, on the basis of the pleadings and such other procedures as it may specify, whether temporary relief should be accorded to any party pending the hearing and the nature of any such temporary relief. Where a petition involves new service to subscribers (other than service coming within the provisions of § 74.1107(a) of this chapter), the Commission will expedite its consideration and promptly issue a ruling either on the merits of the petition or on the interlocutory question of temporary relief pending further procedures.

(g) Where a request for temporary relief is contained in a petition with respect to service coming within the provisions of § 74.1107(d) of this chapter, opposition to such request for temporary relief shall be filed within ten (10) days and reply comments within seven (7) days thereafter. The commission will expedite its consideration of the question of temporary relief.

(h) Where a petition for waiver of the provisions of § 74.1103(a) of this chapter is filed within fifteen (15) days after a request for carriage, the system need not carry the signal of the requesting station pending the Commission's ruling on the petition or on the interlocutory question of temporary relief pending further procedures.

[*Subpart K (§§ 74.1101–74.1109) as adopted eff. 4–18–66, except for § 74.1103 which is eff. 6–17–66 as it pertains to existing operations of nonmicrowave CATV systems and §§ 74.1105, 74.1107, and 74.1109 which are eff. 3–17–66; III(64)–12; § 74.1109(h) as adopted eff. 6–17–66; III(64)–13.*]

No. 22,393

[Uni]ted States Court of Appeals

FOR THE NINTH CIRCUIT

GREAT FALLS COMMUNITY TV CABLE CO., INC.,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION

and

UNITED STATES OF AMERICA,
Respondents,

HARRISCOPE BROADCASTING CORPORATION,
SNYDER & ASSOCIATES,
TELEPROMPTER TRANSMISSION OF KANSAS, INC.,
Intervenors.

On Petition for Review of An Order of the Federal Communications Commission

REPLY BRIEF

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May 17, 1968

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PRELIMINARY STATEMENT

This petition for review generally challenges the jurisdiction of the FCC to regulate CATV, whether microwave fed or off-the-air, and specifically challenges the validity of the CATV non-duplication rules as contained in 47 CFR 21.712 and 74.1103. The challenge against the non-duplication rules are both on constitutional grounds — free speech and due process — and on statutory limitations.

Petitioner moved for a stay of the Commission's order imposing the non-duplication rule, which was granted by order of this Court on January 10, 1968. Respondents in their opposition to the stay asserted that the jurisdiction of the Commission to regulate microwave CATV was "well established", and despite the writ of certiorari to this Court in *Southwestern Cable Co. v. United States*, 378 F.2d 118 (9th Cir., 1967), *cert. granted* 389 U.S. 911 (1967),(reviewing the question of Commission jurisdiction to regulate non-microwave CATV),advised at oral argument through the General Counsel of the FCC that they were prepared to defend their microwave fed CATV jurisdiction here. After a month's extension of time to file their answering brief, respondents have decided not to defend their jurisdiction or make serious response to any of the issues raised in petitioner's brief, but to rely instead upon a procedural challenge of petitioner's right to raise these issues here without first having "afforded the Commission an opportunity to pass upon them".[1] The doctrine upon which respondents rely is misstated in their brief, has no application to the circumstances here, and ignores the controlling rule of this Circuit. Respondents' hyperbole necessitate this reply.

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[1] This is a switch in the Commission's tactics. More often the Commission makes broad explanation and rationale of its jurisdiction in appellate reviews which do not challenge its jurisdiction. In this manner the Commission has had its CATV jurisdiction reasserted in the dicta of opinions, for example, *Wheeling Antenna Co., Inc. v. United States and Federal Communications Commission*, __F.2d__, (4th Cir., decided February 28, 1968). Here, if the Court were to deny jurisdictional review on the procedural ground, no doubt the Commission would cite the opinion as reaffirmance of its assumption of jurisdiction, while never having submitted it to a judicial examination.

ARGUMENT

PETITIONER WAS NOT REQUIRED TO ASSERT BELOW ISSUES REPEATEDLY RAISED BEFORE THE COMMISSION AND SUMMARILY AND CONSISTENTLY REJECTED IN ACCORDANCE WITH ITS FIXED POLICY

Respondents assert that Section 405 of the Communications Act "unequivocally establishes that 'no question of fact or law' may be raised on appeal which petitioner has not first raised before the Commission". The Act does not make such "unequivocal" requirement nor does judicial precedent. Furthermore, the Commission's opportunities to pass upon its jurisdiction over CATV are legion. These opportunities include rulemaking proceedings, court reviews in various circuits and the Supreme Court, applications for waivers of the rules, and a direct challenge by petitioner's parent corporation in separate actions. In each instance the Commission action has been the same. To now assert that the Commission has not had an opportunity to pass upon its jurisdiction is to waste the time of this Court. We review below only a small sample of the opportunities and Commission action.

After a history of denial of its jurisdiction over CATV, jurisdiction was first asserted over microwave-fed CATV in the *First Report and Order,* 38 FCC 683 (1965). The jurisdiction is reasserted and enlarged to cover all CATV in the *Second Report and Order,* 2 FCC 2d 725 at 726 (1966). In answer to petition for reconsideration of the *Second Report,* the Commission again reasserted its jurisdiction with an expanded memorandum on its jurisdiction, 6 F.2d 309 at 310 (1967). Direct reviews of the *First* and *Second Reports* were taken in the D.C. Circuit, the Fifth, Sixth, Eighth and the Ninth Circuits, and consolidated for review in the Eighth Circuit which were submitted in October of 1967.[2] They are yet to be decided.

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[2] The cases are: *Midwest Video, et al v. FCC et al,* No. 18,052, originating in Eighth Circuit; *Midwest Video et al v. FCC et al,* No. 18,348, originating in Eighth Circuit; *Midwest Television, Inc. v. FCC et al,* Nos. 18,481 and 18,482, originating in D.C. Circuit; *Alice Cable*

(Continued)

Petitioner's parent company, TelePrompTer Corporation, participated in both FCC rulemakings which culminated in adoption of the *First* and *Second Reports* on CATV and raised objections based primarily upon First Amendment and jurisdictional grounds — issues passed upon and rejected by the Commission. Indeed, TelePrompTer Corporation, in connection with other of its CATV operations, raised before the Commission *each* of the issues now before this Court and had each repudiated in summary fashion. See Appendix I hereto, reproduced from FCC Reports (7 FCC 2d 604 (1967)) typifying Commission treatment of the questions upon which it now asserts it has had "no opportunity" to pass.

On a test of application of the rules contained in the *Second Report,* this Court placed the Commission's jurisdiction in doubt in *Southwestern Cable Co. v. United States,* 378 F.2d 118 (9th Cir., 1967). Whereupon, the Commission successfully had its jurisdiction reaffirmed in the D.C. Circuit in *Buckeye Cablevision Inc. v. Federal Communications Commission,* 387 F.2d 220 (D.C. Cir., 1967), (where the jurisdictional issue had not been raised by the petitioner),[3] and on the strength of a conflict in circuits the Commission took *Southwestern* to the Supreme Court, *cert. granted,* 389 U.S. 911 (1967).

While this jurisdictional issue has been pending in the courts, the Commission has exercised the disputed jurisdiction with heady confidence. In its standard rebuff to a challenge of jurisdiction, the Commission entones with

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[2] (Continued)
Television Corp. v. FCC et al, No. 18,753, originating in Fifth Circuit; *Buckeye Cablevision, Inc. v. FCC et al,* No. 18,813, originating in Sixth Circuit; and *Mission Cable TV, Inc., et al v. FCC et al,* No. 18,839, originating in Ninth Circuit.

[3] *Buckeye* demonstrates the Commission's tactical skill. In the D.C. Circuit it had its jurisdiction reaffirmed where it had not been challenged on review. Here, the Commission seeks to bar review, where petitioner has squarely raised it, on the grounds that it had not had an "opportunity" to pass upon this issue below.

monotonous regularity from its "boiler plate" opinions[4] that the issue of jurisdiction has been fully disposed of in the *Second Report and Order* and it is unnecessary to reconsider it. Some recent samples from Commission opinions are:

Texas Community Antennas, Inc., __F.C.C.2d __, 12 R.R. 2d 942 (FCC 68-395, April 15, 1968):

> [T]he basis for the Commission's jurisdiction was discussed in the *Second Report and Order* so that it is unnecessary to review it here;. . .

Mountain State Cable, Inc., 9 F.C.C.2d 915 (1967):

> Our reasons for rejecting petitioner's contention that the Commission lacks jurisdiction over off-the-air CATV systems are given in the *Second Report and Order,* and we do not believe they need be repeated here.

Top Vision Cable Co., 8 F.C.C.2d 895 (1967):

> Finally, the *Second Report and Order* and our subsequent reconsideration thereof set forth our grounds for asserting jurisdiction; they need not be repeated here.

TV Transmission, Inc., 6 F.C.C.2d 296 (1967):

> We explained our grounds for asserting jurisdiction over off-the-air CATV systems in the *Second Report and Order,* and we will rely on that discussion in this proceeding.

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[4] Because of the heavy load of matters before it, the Commission for the most part does not write its own opinions. This extraordinary procedure is openly acknowledged and structured in the bureaucratic process by funnelling all matters pending for Commission determination through the Office of Opinions and Review, 47 C.F.R. 0.171, which wades through the pleadings, prepares a proposed opinion and submits this to the Commission, thus relieving the over-taxed Commissioners from the added burden of even reading pleadings.

TelePrompTer Corporation, Santa Cruz, California, 6 F.C.C.2d 299 (1967).[5]

> Furthermore, the Commission is satisfied that the basis for its authority was adequately set forth in the *Second Report.*

Not only has the Commission had more than ample opportunity to pass upon the issues raised here, but it has maintained a frozen attitude to these issues and refuses to give them any examination or response in its opinions. To require petitioner to have challenged the Commission's jurisdiction in its request for waiver would have been idle in the extreme and tactically unsound, since it would have jeopardized a case on the merits.

In addition to ample opportunity to pass upon its jurisdiction, it is well established that subject matter jurisdiction can be raised at any judicial level. In *Mansfield, Coldwater & Lake Michigan Railway Company v. Swan,* 111 U.S. 379 at 382 (1884) the Court explained:

> On every writ of error or appeal, the first and fundamental question is that of jursidiction, first, of this court, and then of the court from which the record comes. This question the court is bound to ask and answer for itself even when not otherwise suggested, and without respect to the relation of the parties to it.

Unlike jurisdiction over the parties, subject matter jurisdiction cannot be waived, *People's Bank v. Calhoun,* 102 U.S. 256, 260-261 (1880); *Page v. Wright,* 116 F.2d 449, 453 (7th Cir., 1940). Moreover, a party cannot be estopped from raising a want or jurisdiction. *American Fire & Casualty Co. v. Finn,* 341 U.S. 6, 17-18 (1951). Jurisdiction can

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[5] This latter case was asserted by petitioner's parent corporation. See also *TeleprompTer Corporation* 7 FCC 2d 604 (1967), set forth in Appendix I hereto.

even be raised by the party who in the first instance invoked the Court's jurisdiction, *American Fire & Casualty Company v. Finn, supra,* and the court may on its own motion demand that jurisdiction be clearly demonstrated even when not raised by the parties, *McNutt v. General Motors Acceptance Corporation,* 298 U.S. 178 (1936). Thus, it is clear that the Commission's jurisdiction is a necessary issue before this Court.

Likewise, the constitutional issue of free speech has been passed upon by the Commission and is properly at issue here. The free speech issue was passed upon by the Commission in the *Reconsideration of the Second Report and Order,* 6 FCC 2d 309 at 310 (1967). Also, it has frequently been raised before the Commission and rejected out of hand by citing the *Second Report* as the sole authority. *Helena Television Co.,* __FCC 2d __, 12 R.R.2d 1163 (FCC 68-422, decided April 22, 1968); *Texas Community Antennas, Inc.,* __FCC 2d __, 12 R.R.2d 942 (FCC 68-395, decided April 15, 1968); *Allen's Television Service, Inc.,* __FCC 2d __, 12 R.R.2d 1030 (FCC 68-399, decided April 15, 1968); *Ellensburg Television Cable Corp.,* 7 FCC 2d 110 (1967); *Minnesota CATV, Inc.,* 7 FCC 2d 943 (1967); *TelePrompTer Corp.,* 7 FCC 2d 604;[6] *Total Telecable, Inc.,* 7 FCC 2d 611 (1967), now on review before this Court,in No. 21,990.

The same is true with respect to Commission's review and rejection of the right to hearing in a waiver petition. *Texas Community Antennas, Inc.,* __FCC 2d __, 12 R.R.2d 942 (FCC 68-395, April 15, 1968); *Allen's Television Service, Inc.,* __F.2d __, 12 R.R.2d 1030 (FCC 68-399, April 15, 1968); *TelePrompTer of Liberal, Inc.,* 8 FCC 2d 473 (1967); *Douglas Antenna Cable TV,* 8 FCC 2d 317 (1967); *Ellensburg Television Cable Corp.,* 7 FCC 2d 110 (1967); *Minnesota CATV, Inc.,* 7 FCC 2d 943 (1967); *TelePrompTer Corporation,* 7 FCC 2d 604 (1967); *Total Telecable, Inc.,* 7 FCC 2d 611 (1967); *TelePrompTer of Liberal,*

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[6] Set forth in full in Appendix I hereto.

Inc., 7 FCC 2d 120, (1967); *Tehachapi TV Cable Co.*, 6 FCC 2d 469 (1967); *Total Telecable, Inc.*, 8 FCC 2d 997 (1967). In fact each issue which has been raised in this review is examined in both the majority and dissenting opinions of the *Second Report and Order, supra,* and have been separately asserted before the Commission by petitioner's parent and affiliated corporations.

Without stating by name, the respondents apparently rely upon the doctrine of exhaustion of administrative remedies before seeking review in the courts. The confused opinions in this area are weighed by Professor Davis in his authoritative study of administrative law (3 Davis, *Administrative Law* 67, §20.03):

> As we have just seen, the Supreme Court cases go both ways on the question whether administrative jurisdiction may be challenged without exhausting administrative remedies. Not only are the holdings often irreconcilable, but no opinion of the Court explains the contrariety of holdings. Indeed, the word formulations in the opinions are inadequate, conflicting, and usually affirmatively misleading.

Professor Davis suggests a way out of the darkness by making the requirement of prior administrative review dependent upon three key factors (3 Davis, *Administrative Law* 69):

> . . . [E]xtent of injury from pursuit of administrative remedy, degree of apparent clarity or doubt about administrative jurisdiction, and involvement of specialized administrative understanding in the question of jurisdiction.

These guidelines have been adopted by this Court in *Lone Star Cement Corporation v. Federal Trade Commission*, 339 F2d 505 (9th Cir., 1964), cited with favor by Professor Davis in the pocket supplement to Section 20.03 of his text. When applied to this review they support a full review of the issues pending before the Court.

First, the issue of administrative jurisdiction in the Commission's view has been definitively resolved and the result of any submission of this issue is a foregone conclusion. Where submission to the agency constitutes only an idle act or a mere formality it is not a prerequisite for review. *Levers v. Anderson*, 326 U.S. 219, 222-223 (1945). The law generally does not require a party to perform an idle act.

Secondly, the issues to which the Commission seeks to foreclose examination are for the most part beyond the ambit of the Commission's technical expertise or specialized knowledge. There are no factual issues requiring Commission resolution, nor are there legal issues within its special administrative knowledge. Statutory construction and constitutional issues of free speech and due process are issues more appropriate to the consideration of the courts. *Public Utilities Commission of California v. United States*, 355 U.S. 534, 539-540 (1958); *Chicago v. Atchison Topeka & Santa Fe Railway Co.*, 357 U.S. 77 (1958).

And lastly, the petitioner has demonstrated in its application for stay that enforcement of the Commission order would cause it irreparable harm. The Commission resisted the stay in this Court despite the absence of any corresponding compelling reasons for enforcement. From this Commission intransigence and past performance (including a denial of a stay of the *Second Report and Order* itself,pending reconsideration. 3 F.C.C.2d 816 (1966)) it is logical to infer that the Commission would have denied a stay[7] to petitioner during the pendency of a petition for reconsideration before it – a period frequently in excess of a year, even when decided without examination. Thus, the only possible avoidance of irreparable harm was to immediately proceed in this Court.

---

[7] Filing of a petition to reconsider under the Commission's rules does not stay its order, 47 C.F.R. 1.108(n).

Section 405 of the Communications Act does not require that the petitioner assert his grounds before the Commission to preserve them for review. It states only that the Commission shall have been afforded an opportunity to pass upon them. The myriad of such opportunities have been demonstrated above. Additionally, the exceptions to this statutory statement of exhaustion of administrative remedies has been examined above. Furthermore, the cases upon which respondents principally rely assert no such inflexible rule.

CONCLUSION

For the foregoing reasons, respondents' argument of exhaustion of administrative remedies is without substance or merit.

Respectfully submitted,

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May 17, 1968

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ Alan Raywid

FCC 67-393

BEFORE THE

FEDERAL COMMUNICATIONS COMMISSION

WASHINGTON, D.C. 20554

In re
TELEPROMPTER CORP., JOHNSTOWN, PA., AND ELMIRA, N.Y.
Request for Waiver of Section 74.1103 of the Commission's Rules

MEMORANDUM OPINION AND ORDER

(Adopted March 29, 1967)

BY THE COMMISSION: COMMISSIONER BARTLEY DISSENTING AND ISSUING A STATEMENT; COMMISSIONER LOEVINGER CONCURRING IN THE ORDER; COMMISSIONER JOHNSON ABSENT.

1. On June 17, 1966, TelePrompTer Corp., owner and operator of CATV systems in Johnstown, Pa., and Elmira, N.Y., filed a petition to set aside, stay, annul, suspend, and/or waive CATV nonduplication rules, in which it requested waiver of the program exclusivity requirements of section 74.1103(e) of the Commission's rules. Oppositions to the Johnstown request were filed by Rivoli Realty Co., permittee of station WARD–TV, and WJAC, Inc., licensee of station WJAC–TV, both in Johnstown, Pa.; opposition to the Elmira request was filed by Newhouse Broadcasting Corp., licensee of UHF station WSYE–TV, Elmira, N.Y.; and Triangle Publications, Inc., licensee of stations WFBG–TV, Altoona, Pa., and WNBF–TV, Binghamton, N.Y., filed an opposition addressed to both requests. TelePrompTer replied.

2. TelePrompTer, through its wholly owned subsidiary Johnstown Cable TV, operates a 5-channel off-the-air CATV system in Johnstown, Pa., which supplies approximately 10,470 subscribers with the following Pennsylvania television signals: KDKA–TV (CBS), WTAE (ABC), and WIIC–TV (NBC), Pittsburgh; WFBG–TV (ABC, CBS), Altoona; WJAC–TV (NBC) and WARD–TV (CBS), Johnstown. Stations WFBG–TV, WJAC–TV, and WARD–TV provide predicted grade A contours, and stations KDKA–TV, WTAE, and WIIC–TV provide predicted grade B contours over Johnstown. Similarly, through its wholly owned subsidiary, Elmira Video, TelePrompTer operates a 12-channel CATV system in Elmira, N.Y., which supplies approximately 16,041 subscribers with the following signals: Off-the-air—WINR–TV (NBC), WNBF–TV (CBS), and WBJA–TV (ABC), Binghamton; WSYE–TV (NBC), Elmira; WHEN–TV (CBS) and WNYS–TV (ABC), Syracuse, all New York; WDAU–TV (CBS), Scranton, Pa.; via microwave [1]—independent

[1] In its waiver request, the petitioner indicated that it did not employ microwave; however, we rely on its later-filed form 325 which indicates that it now does so.

stations WPIX, WOR-TV, and WNEW-TV, from New York City
Stations WNBF-TV and WSYE-TV provide predicted grade A con
tours, and station WBJA-TV provides a predicted grade B contou
over Elmira. TelePrompTer requests a blanket waiver of sectio
74.1103(e) of the rules for both the Johnstown and Elmira CAT
systems in order to avoid furnishing program exclusivity.

3. In support of its waiver request, TelePrompTer urges: (*a*) Tha
in view of the copyright decision in *United Artists Television, Inc.*
Fortnightly Corporation, 255 F. Supp. 177, appeal pending before th
U.S. Court of Appeals for the Second Circuit (docket No. 30767),
broadcaster should not be entitled to assert its rights under sectio
74.1103 of the rules without first agreeing to indemnify a CATV ope
ator for its potential copyright liability; (*b*) that the broadcaste
should be required to pay the CATV operator's cost resulting fro
implementation of program exclusivity; (*c*) that section 74.1103 of th
rules should not be applied without first affording the CATV operat
a hearing; (*d*) that the application of section 74.1103 of the rul
would inhibit the distribution of constitutionally protected materi
(under the first amendment to the Constitution of the United States
as well as violate section 326 of the Commission's act, and the Com
mission has never decided whether it possesses authority to restra
distribution of constitutionally protected communications whe
radio stations are not involved; and (e) that since it has been hel
that a CATV system's operation does not constitute "unfair compet
tion," citing *Cable Vision, Inc.* v. *KUTV, Inc.*, 335 F. 2d 348, cert. den
379 U.S. 989, this is an improper basis for the Commission's assertio
of jurisdiction.

4. TelePrompTer's arguments are considered sequentially belo
(*a*) No question of copyright liability can arise where, as here, onl
deletion of a program from a CATV system is at issue; (*b*) the burde
of a governmentally imposed expenditure upon an industry is not v
olative of the fifth amendment where the end result is legitimate an
the means are rational. See, e.g., *Day-Brite Lighting, Inc.* v. *Missou*
342 U.S. 421; *California State Auto. Ass'n Inter-Insurance Bureau*
Maloney, 341 U.S. 105; *Buchwalter* v. *Federal Trade Commission*, 2
F. 2d 344. Moreover, TelePrompTer had the opportunity to parti
ipate in the rulemaking and was on notice that it would be affecte
when the rules went into operation; (*c*) section 74.1109(f) of the rul
makes provision for hearings; however, TelePrompTer's thresho
factual allegations do not persuade us that a hearing is necessary her
(*d*) this question was considered and disposed of on reconsiderati
of the *Second Report and Order* and we rely on our discussion ther
paragraph 2 et seq., FCC 67-34, 6 FCC 2d 309; (*e*) the *KUTV* ca
did not consider or purport to deal with the unfair competition aspe
developed in the *Second Report and Order* under the public-intere
standard of the Communications Act of 1934, as amended. That ca
simply held that parties in a private suit must proceed under cop
right law, rather than on the concept of unfair competition or inte
ference with contractual rights, in view of such decisions as *Sea*
Roebuck & Co. v. *Stiffel Co.*, 367 U.S. 225, and *Compco Corp.* v. *Da*
Brite Lighting, Inc., 376 U.S. 234.

5. In view of the foregoing, the Commission finds that a grant of the requested waiver of section 74.1103(e) of the Commission's rules would not be consistent with the public interest.

Accordingly, *It is ordered*, This 29th day of March 1967, that the petition to set aside, stay, annul, suspend, and/or waive CATV nonduplication rules, filed by TelePrompTer Corp. on June 17, 1966, requesting waiver of section 74.1103(e) of the Commission's rules as it relates to the petitioner's operation of Johnstown Cable TV, Johnstown, Pa., and Elmira Video, Elmira, N.Y., *Is denied*.

It is further ordered, That TelePrompTer Corp. *Is directed* to comply with the requirements of section 74.1103(e) of the Commission's rules on its CATV systems described above within 30 days of the release date of this memorandum opinion and order.

FEDERAL COMMUNICATIONS COMMISSION,
BEN F. WAPLE, *Secretary*.

DISSENTING STATEMENT OF COMMISSIONER ROBERT T. BARTLEY

In my opinion, the CATV rules are invalid and waivers are not necessary. However, assuming their validity, I would here grant full relief as requested by the CATV.

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Respondents,

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On Petition for Review of an Order of the Federal Communications Commission

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SUPPLEMENTAL BRIEF FOR PETITIONER

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July 17, 1968

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On Petition for Review of an Order of the Federal Communications Commission

SUPPLEMENTAL BRIEF FOR PETITIONER

PRELIMINARY STATEMENT

This review has been briefed and argument is set for July 24, 1968. By order of the Court of June 25, 1968, leave was granted for the simultaneous filing of supplemental

briefs to discuss the impact on the pending review of the Supreme Court's decisions in both *United States v. Southwestern Cable Co.*, 392 U.S.___, 36 U.S.L.W. 4553 (No. 363, June 10, 1968) and *Fortnightly Corp. v. United Artists Television, Inc.*, 392 U.S.___, 36 U.S.L.W. 4656 (No. 618, June 17, 1968). We review these decisions here. 1/

ARGUMENT

I

In *United States v. Southwestern Cable Co.*, *supra.*, the Supreme Court squarely upheld the jurisdiction of the Federal Communications Commission to regulate CATV, whether off-the-air or microwave fed, under the Commission's authority to regulate communications by wire or radio. But in its broad jurisdictional affirmance the Court stressed that it was not passing upon or examining the CATV rules promulgated under this authority (Id., at 4556):

> We must first emphasize that questions as to the validity of the specific rules promulgated by the Commission for the regulation of CATV are not now before the Court.
> . . . .

1/ Counsel for petitioners also appear and advance similar arguments in *Total Telecable, Inc. v. Federal Communications Commission*, No. 21,990, now pending before this Court for decision.

Nor did the Court outline the limits or extent of the Commission's regulatory power over CATV. (Id., at 4559):

> There is no need here to determine in detail the limits of the Commission's authority to regulate CATV. It is enough to emphasize that the authority which we recognize today under §152(a) is restricted to that reasonably ancillary to the effective performance of the Commission's various responsibilities for the regulation of television broadcasting. The Commission may, for these purposes, issue "such rules and regulations and prescribe such restrictions and conditions, not inconsistent with law", as "public convenience, interest or necessity requires". 47 U.S.C. §303(r). We express no views as to the Commission's authority, if any, to regulate CATV under any other circumstances or for any other purposes.

Thus, the issues before this Court in the instant review challenging the Commission's jurisdiction over CATV (Argument, parts I and II) are moot. Remaining, however, are the specific challenges of the validity of the non-duplication rules, 47 C.F.R. §§ 21.712 and 74.1103 (Argument, part III); challenge of the absence of guarantees in the rules to provide for an evidentiary hearing before curtailing existing service under Section 74.1109 of the rules (part IV); and the challenge of the reasonableness of the non-duplication rules acting in restraint of trade (part V). These challenges raise constitutional and

statutory questions not before the Supreme Court, but raised here. We examine below the Court's decision in the two cases insofar as they bear upon the constitutional and statutory questions at issue here.

II

The non-duplication rules, Sections 21.712 and 74.1103, provide for *same-day* non-duplication of the programs of local stations by more distant stations also carried by the CATV system. We argue in Part III of our Brief that the Commission's order of non-duplication imposes a prior restraint upon the *reception* and *distribution* of information in violation of free speech guarantees of the First Amendment. Language in the Supreme Court's recent decisions confirms our factual analysis of the type of service provided by the CATV system. Broadcasting contents are "a principal source of information and entertainment" *Southwestern, supra,* at 4559. Television viewing is achieved by both broadcaster who transmits signals and viewers, who "by means of television sets and antennas that they themselves provide, receive the broadcasting signals and reconvert them into the visible images and audible sounds of the program." *Fortnightly, supra.,* at 4658. The service provided by CATV in television is

ordinarily a "simultaneous retransmission of communications" in a stream that is "essentially uninterrupted and properly indivisible." *Southwestern, supra,* at 4557.

Both decisions by the Supreme Court recognize CATV operation as essentially *receipt* and *distribution* of program materials. Insofar as a "performance" under the Copyright Act is concerned, *Fortnightly* held that the CATV service more closely resembles the viewer's role than the broadcaster's (Id., at 4658-4659):

> Broadcasters procure programs and propagate them to the public; CATV systems *receive* programs that have been released to the public and carry them by private channels to additional viewers. We hold that CATV operators, like viewers and unlike broadcasters, do not perform the programs that they receive and carry. [Emphasis added.]

Of course, the CATV rules themselves acknowledge that CATV service essentially "receives" and "distributes" signals in §74.1101, "Definitions",and in the caption of the carriage and non-duplication rule, §74.1103: "Requirement relating to *distribution* of television signals by community antenna television systems." [Emphasis added.] Thus, if our analysis in part III of our Brief is correct that the constitutional protection of free speech includes

the right to distribute and the right to receive, the CATV receipt and distribution of broadcast signals is squarely within the First Amendment protection.

The Commission has argued that "reasonable regulation of the use of the *radio spectrum*" [emphasis added] has been held not in violation of free speech under the First Amendment in *National Broadcasting Co. v. United States*, 319 U.S. 190, 217 (1943) (Government Brief, part III, p. 17). But the Supreme Court in *Fortnightly* has held the CATV service more closely akin to the viewers' function than the broadcasters', and thus the analogy to broadcasting regulation fails. Moreover, CATV in receipt and distribution makes no use of "spectrum space" and the underpinning of reasonable regulation similarly fails. In preserving scarce spectrum space the Commission through its licensing actually promotes the exercise of free speech, since if everyone were to broadcast no one could be heard. Commission reliance on *NBC, supra,* as authority for prior restraint of CATV carriage is misplaced, since CATV service occupies no spectrum space. Unlike the broadcast licensing rules, the non-duplication rules do not promote free speech and

are unreasonable.[2/]

Indisputably *same-day* non-duplication limits and restricts access to available information and materials provided by the broadcaster. We concede that *simultaneous* non-duplication limits only the available *source* or channel of program materials. But *same-day* duplication protection, as required by the rules, directly restricts the availability and the viewer's choice of program materials. For example, when two nationally attractive network shows are simultaneously pitted against each other (such as Huntley-Brinkley and Walter Cronkite) the viewer cannot witness both. However, if CATV carriage brings these programs from a different time zone (as here) or merely brings programs broadcast at different times from a nearby station within the same time zone, the viewer's access to information and materials is widened. Additionally, the viewer's

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2/ However, the Tenth Circuit in a recent opinion has held non-duplication protection is reasonable regulation and not in violation of the First Amendment. *Conley Electronics Corp. v. Federal Communications Commission.*, __F.2d__, 12 R.R.2d 2108 (Tenth Circuit 1968). We feel that the Tenth Circuit failed to distinguish between the bases for regulation of broadcasting and CATV. Preservation of spectrum space as a reasonable basis for broadcasting regulation sheds no light on the reasonableness of prior restraint of CATV programs. The Tenth Circuit has been asked to stay its mandate pending a filing of a petition for certiorari.

own convenience or availability may be at one broadcast time and not the other. Or, he may wish to watch the same program twice. In each of these instances, the Commission's rule restricts his right to receive and the CATV systems' right to distribute, and thus constitutes a prior restraint upon the flow of information.

The Commission has repeatedly stated that the Communications Act does not permit it to limit or select program sources or materials. Indeed, the act expressly prohibits this function under 47 U.S.C. §326, the censorship provision. Most recently the Commission in official action advised the National Commission on the Cause and Prevention of Violence that the Commission was reluctant to undertake studies on the causal connection between violence and broadcast materials "because we are the licensing agency for the stations involved and are hesitant about encroaching on their freedom of program choice." FCC 68-622, Mimeo No. 16828, dated June 12, 1968. If the Commission is powerless to limit the broadcasters' "freedom of program choice" even when it may endanger the public safety, then *a fortiori* it is powerless to limit the choice of available materials broadcasted to members of the viewing public, or the right of the CATV system to carry the available signals.

The only exercise of review over television program materials by the Commission has been through grant or renewal of licenses in comparing the service offered by competing broadcast applicants. Denial of an application for a license for a radio station under this accepted system of licensing, has been held to be no impairment of First Amendment freedom. However, there is no precedent supporting FCC's proscription of distribution of communications over closed-circuit cable facilities for which no federal license is required. And the FCC cannot lawfully condition the public's guaranteed access to broadcast materials upon relinquishment of the constitutional right to distribute or receive free of governmental restraint.

Southwestern and *Fortnightly* properly characterize CATV service as essentially reception and distribution of available broadcast signals. Moreover, *Fortnightly* permits use of the available material free of any copyright infringement. More important than access to copyright material is the protection of freedom of speech and the access to available information and materials. *Same-day* non-duplication protection infringes upon this right.

III

We urged in Part IV of our Brief that the Commission's summary order limiting and curtailing an existing service violates the due process clause of the Fifth Amendment and is in conflict with pertinent statutes and regulations. In support of this contention we cited this Court's opinion in *Southwestern Cable Co. v. United States*, 378 F.2d 118 (9th Cir., 1967). In reversing this Court's opinion, the Supreme Court noted that there is no claim that the Commission's "procedure in this respect is in any way constitutionally infirm." *United States v. Southwestern Cable Co.*, 392 U.S. __, 36 U.S.L.W. 4553, at 4560 (No. 363, June 10, 1968). Further, the Court in upholding the Commission's summary procedure in freezing service, held that Section 312 of the Communications Act, the cease and desist provision, did not apply, since the question before the Commission was "only whether an existing situation should be preserved pending a determination 'whether respondents' present or planned CATV operations are consistent with the public interest.'" (Id., at 4560). Rather than a cease and desist order, the Commission's order was designed "simply to preserve the situation as it existed at the moment of issuance." *Ibid.*

Here, the circumstances are manifestly different. Petitioner's existing service and carriage of the disputed signals pre-date promulgation of the Commission's CATV regulations. Because petitioner was in operation before March 17, 1966, under the rules it is conferred "grandfather rights" for the carriage of distant signals, §74.1105. However, under the Commission's order of compliance with its rules, it must hald carriage of *same-day* duplicating programs--a substantial curtailment of existing service. Petitioner has asserted that the ordered diminution in service will cause a corresponding decline in subscription and threatens existence of the system. Additionally, petitioner has asserted that the maintenance of the duplicating signals has not and will not cause harm to the economic viability of local television. The CATV rules are premised on findings contrary to these assertions, i.e., that non-duplication protection does not harm the CATV, and that failure to provide it is harmful to the TV station. Petitioner maintains that irrespective of what regulations the Commission may impose on new or existing service, it may not halt existing service without demonstrating in an evidentiary hearing that the premises for its rules have application to the particular

operation. Petitioner argues that this right is constitutionally guaranteed by the due process clause of the Fifth Amendment. Moreover, if Commission licensees are given this right under §312 of the Act, non-licensees have at minimum similar rights and protections. *Southwestern* does not hold to the contrary; rather it supports petitioner's claim, since the Court there took such pains to exclude a §312 situation on the ground that the case before it halted only an *extension* of future service, not a curtailment or restriction of existing service. Accordingly, the Supreme Court's affirmance of the Commission's jurisdiction and the right to certain summary proceedings applicable to new service or the freezing of existing service, does not diminish petitioner's right to due process and an evidentiary hearing on the roll back of its service which predates the rules.

IV

We urge in Part V of our Brief that the non-duplication rules are an unreasonable and arbitrary restriction in restraint of trade beyond the legislative

purposes of the Communications Act.[3/] *United States v. Southwestern Cable Co., supra* without delineating the bounds of such regulation, holds that the Commission may regulate CATV. The Supreme Court observed that the rules provide for non-duplication protection (Id., at 4556) and that in formulation of the rules the Commission found that "'CATV competition can have a substantial negative effect upon station audiences and revenues . . ..'" (Id., at 4555). Beyond these observations, *Southwestern* says no more with respect to the Commission's finding or the validity of the rule issued. However, *Fortnightly v. United Artists Television, Inc.*, 392 U.S.__, 36 U.S.L.W. 4656 (No. 618, June 17, 1968) holds that CATV carriage of television signals is not a copyright infringement under the Copyright Act. The Commission's finding of unfair competition is thus weakened, since the carriage of TV materials is a legitimate viewing and distribution of available information and materials. (See p. 75 of our Brief).

3/ For a thoughtful analysis of public interest considerations in maintenance of free competition in the regulated industries see *Northern Natural Gas Company v. Federal Power Commission*, __F.2d__, (D.C. Circuit, No. 21,333, decided June 21, 1968).

Remaining for determination by this Court in light of the characterization of CATV functions in *Fortnightly* is whether *same-day* non-duplication unfairly and unreasonably acts in restraint of trade to the prejudice of the public interest. We maintain that it does. Jurisdiction to regulate CATV in the public interest is not blanket authority to free television from competition nor to limit market entry or impose restrictive regulation to broadcasting competition. The Federal Communications Commission would better exercise its newly found jurisdiction in the public interest by regulating so as to promote competition and to broaden the choice and availability of information and materials.

CONCLUSION

For the foregoing reasons, petitioner prays that the Court vacate the Commission order herein and that it hold invalid *same-day* non-duplication, under §74.1103, or in the alternative that it declare that petitioner is entitled to an evidentiary hearing before imposing non-duplication protection.

Respectfully submitted,

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July 17, 1968

BRIEF FOR RESPONDENTS

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ORDER OF THE FEDERAL COMMUNICATIONS COMMISSION

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ON PETITION FOR REVIEW OF A MEMORANDUM OPINION AND
ORDER OF THE FEDERAL COMMUNICATIONS COMMISSION

BRIEF FOR RESPONDENTS

COUNTERSTATEMENT OF THE CASE

Petitioner, Great Falls Community Cable Company, Inc., operates a CATV system in Great Falls, Montana, using the services of microwave common carriers licensed by the Federal Communications Commission to import distant signals into its community. Before the Commission Great Falls sought a partial waiver of rules and regulations which require the licensed carriers and petitioner's CATV system not to import distant signals which duplicate programs to be carried by the local television stations in Great Falls

during the same day. When the Commission denied the waiver (R. 80-84), it sought review in this Court pursuant to Section 402(a) of the Communications Act, 47 U.S.C. 402(a).

The basic facts are undisputed: Great Falls operates a CATV system in Great Falls, Montana. A CATV system receives and amplifies signals of distant television stations and distributes them by cable to homes of individual subscribers who pay a monthly fee. Petitioner receives its distant signals by means of microwave facilities licensed by the Commission. This permits Great Falls to import into its community six distant signals; one from Canada, two from Salt Lake City, Utah, and three from Spokane, Washington. Great Falls, Montana, has two local television stations of its own, KFBB-TV and KRTV. These, too, are carried on petitioner's system.

Section 74.1103 of the Commission's rules, 47 CFR 74.1103 (1967 Supp.), requires that the CATV system refrain from duplicating on the same day any program broadcast by the two local television stations. In other words, where a program is to be carried by both a distant station and a local station, the rule simply requires that the CATV system give preference to the local station's programs. The community itself would continue to receive <u>all</u> the programs carried by the system, but in some instances a choice of viewing times would be eliminated. A

similar rule, 47 CFR §21.712, applies to the licensed microwave common carriers, which the system uses to import the distant signals. The carrier, TelePrompTer Transmission of Kansas, Inc., is affiliated with the CATV system.

In its pleadings before the Commission, petitioner and its affiliated carrier asked for a partial waiver of the non-duplication rule. After considering all of the pleadings, including objections by the local television stations, the Commission denied the request. It observed that the arguments in support of a waiver "center around viewing time alternatives and CATV service disruption, and were specifically dealt with in the Second Report and Order. Same-day program exclusivity is designed in part to deal with the very situation which petitioner would have us maintain, i.e., CATV importation of programs from an adjoining time zone which duplicate local stations' network programs an hour or two after they are presented locally." (R. 68)[1/]

1/ Petitioner asserts before this Court that enforcement of the non-duplication order will "eliminate about 60 percent of the service" of its system. This assertion is inaccurate, misleading, and simply not in accordance with the record facts, i.e., petitioner's showing before the agency (R. 11-17). Thus, petitioner's own showing establishes that on Sunday, February 13, the day offered as an example of the impact the rule would have on its system (R. 40) petitioner would have to delete 23 program hours (R. 11) out of a total programming schedule of some 107 hours (R. 11, 17). But this is less than 25% of all the programs carried on petitioner's system on Sunday. The 60% figure apparently applies to a limited 2 hour segment from 8:00 to 10:00 P.M. (R. 40), during which time it would have to delete network programs like "Bonanza" and "Ed Sullivan." But these programs would still be available on the system as broadcast by the local stations. (R. 11).

In its pleadings before the Commission Great Falls and its affiliate did not challenge the validity of the Commission's CATV rules, or its jurisdiction to regulate CATV. (See R. 2-26, 37-[illegible]). Since its appeal brings these questions into issue, it would be useful, we believe, to set forth briefly the principal considerations which led to the adoption of the non-duplication rule.

In the First Report and Order, 38 F.C.C. 683, the Commission observed that the national television system is based upon the distribution of programs to the public through a multiplicity of local station outlets, and that this policy had been recently reaffirmed by the Congress (38 F.C.C. 697, pars. 40-47). CATV, while useful as an auxiliary service, must have a complementary role to the television broadcast station for the following reasons (38 F.C.C. 699, pars. 44-45):

(1) CATV cannot serve many persons reached by television broadcast signals because of the prohibitive costs of extending cable beyond heavily built-up areas. This means that people living outside heavily populated areas and those who cannot afford or do not wish to pay are entirely dependent upon local stations for television service. Primary reliance cannot therefore be placed on the CATV since it is a "service which, technically, cannot be made available to many others."

(2) Local stations serve as outlets for community self-expression, presenting programming designed to serve the needs and interests of local areas. Conversely, most CATV systems do not originate any local programming.

Having concluded that CATV serves the public interest "when it acts as a supplement rather than a substitute for off-the-air television service" (38 F.C.C. 701, par. 48), the Commission turned to the basic conditions under which competition between the CATV and the local television station occurs (38 F.C.C. 701-706, pars. 49-57 [2/]). It found that the competition was marked by features not present in the ordinary competition between broadcast stations, which were both unfair and inconsistent with the CATV's proper role as a supplementary service. The Commission noted that there has developed, under both the Communications Act and the antitrust laws, a reasonable amount of exclusivity on the exhibition of TV programs within the station's market and for a particular time period (38 F.C.C. 703, pars. 52-53). CATV, however, presently stands outside the established program distribution process and brings into a local station's area the programs of distant stations, irrespective of the reasonable exclusivity which the local station has bargained for in the competitive TV market. (38 F.C.C. 704, par. 54)

2/ The two compete because when a cable system brings to a station's market additional signals which would not be readily available in the system's absence, it introduces competition for audience attention--and audience attention is the basic commodity that a station sells to advertisers. 38 F.C.C. 702, par. 50.

In addition to the above considerations, the Commission considered the question of the impact of CATV competition on the development of television broadcasting service (38 F.C.C. 706-713, pars. 58-75). It analyzed the economic data which had been presented and took into account information which had been acquired in case to case adjudication (38 F.C.C. 708-711, pars. 64, 68-69). Noting the explosive growth of CATV and its changing nature (38 F.C.C. 709, par. 65), as well as the increasing penetration of television stations' service areas (38 F.C.C. 709-710, pars. 66-67), the Commission concluded that remedial action was warranted (38 F.C.C. 713-15, pars. 76-79).

It therefore adopted Section 21.712, 47 CFR 21.712, its carriage and nonduplication rules for microwave-served CATV systems. 3/ The need for such rules was reaffirmed in the Second Report and Order (2 F.C.C. 2d at 745-56, pars. 47-75) where the Commission broadened the scope of the regulations to include all CATV systems, finding them "essential to insure that CATV continues to perform its valuable supplementary role without unduly damaging or impeding the growth of television broadcast service" (2 F.C.C. 2d 746, par. 47).

The nonduplication rule provides that upon request by the local station a CATV must not duplicate programs broadcast by the local station during the same day. Thus it gives a

3/ Section 74.1103 is the corresponding rule for non-microwave-served CATV systems. The two rules are identical in substance, and are hereafter referred to as the nonduplication rule. They are set forth in the Appendix for Petitioner at 89A-96A.

preference to carriage of local signals by the CATV over distant signals where the programming is the same. The rule, however, specifies a number of exceptions. Thus, nonduplication protection applies to "prime time" network programs (i.e., those presented by the network between 6 p.m. and 11 p.m.) only if such programs are presented by the local station entirely within what is locally considered to be "prime time". Furthermore, a local station is only entitled to nonduplication protection against "more distant duplicating signals, but not against signals of equal priority * * *." Finally, the CATV system need not delete reception of a network program if, in doing so, it would leave available for reception of subscribers, at any time, less than the programs of two networks, or would deprive them of color reception of the program.

QUESTIONS PRESENTED

Respondents believe that a threshold question presented by this appeal is:

Whether Section 405 of the Communications Act, 47 U.S.C. 405 bars review of petitioner's claims of error since they were not raised before the Commission.

If the Court should find that the issues raised by petitioner are properly before it, we believe the questions presented may be stated as follows:

Whether the Commission has the authority to require that CATV systems which are served by FCC-licensed microwave facilities must, in order to receive that service, afford nonduplication to local stations.

Whether the nonduplication provision is an unconstitutional restriction on free speech.

Whether the nonduplication rule is reasonably related to the public interest standard of the Communications Act.

Whether an evidentiary hearing was required on petitioner's request for a waiver of the rule.

ARGUMENT

I. SECTION 405 OF THE COMMUNICATIONS ACT PRECLUDES REVIEW OF CONTENTIONS NOT RAISED BEFORE THE COMMISSION. SINCE NONE OF PETITIONER'S ARGUMENTS WERE RAISED BELOW, THEY ARE NOT PROPERLY BEFORE THE COURT.

In its brief Great Falls has launched a wide ranging general attack on the validity of all the Commission's CATV regulations and on the Commission's jurisdiction to regulate CATV. Before the Commission it did not raise any of its present contentions. Instead it tried to justify a partial waiver of the non-duplication rule based upon alleged hardships which would result from strict application of the rule (R. 2-9; 15-26; 37-43). Great Falls is therefore precluded from raising these matters for the first time on appeal.

Section 405 of the Communications Act, 47 USC §405, unequivocally establishes that no "question of fact or law" may be raised on appeal which petitioner has not first raised before the Commission.[4/] See also United States v. Tucker Truck Lines, 344 U.S. 33 (1952); Unemployment Commission v. Aragon, 329 U.S. 143, 155 (1946); Albertson v. F.C.C., 243 F.2d 209 (C.A.D.C. 1957); Florida Gulfcoast Broadcasters v. F.C.C., 352 F.2d 726 (C.A.D.C. 1965).

4/ In pertinent part 47 U.S.C. 405 states:

> A petition for rehearing must be filed within thirty days from the date upon which public notice is given of the order, decision, report, or action complained of. . . . The filing of a petition for rehearing shall not be a condition precedent to judicial review of any such order, decision, report, or action, except where the party seeking such review (1) was not a party to the proceedings resulting in such order, decision, report, or action, or (2) relies on questions of fact or law upon which the Commission, or designated authority within the Commission, has been afforded no opportunity to pass.

In view of these authorities, it is clear beyond question that petitioner's claims with respect to the First Amendment (Br. pp. 44-49), the need for an evidentiary hearing (Br. pp. 49-63), and the alleged arbitrary nature of the rule are properly outside the scope of this appeal. The record below is silent on these points since they were not asserted by petitioner and there is therefore nothing for this Court to review. Indeed, even as to the question of the Commission's jurisdiction (Br. pp. 10-40), it has been held that 47 U.S.C. §405 requires as a condition precedent to judicial review that the matter be raised before the agency. Presque Isle TV Co., Inc. v. United States, 387 F.2d 502, 504-506 (C.A. 1, 1967).

In that case the First Circuit held that a claim that the Commission lacks jurisdiction to regulate CATV was not properly before it because it had not been expressly presented to the Commission. After reviewing the relevant authorities in considerable detail, the Court concluded:

> We hold that even though the question of statutory interpretation was, strictly, a jurisdictional matter, it was a question of law which petitioners were obliged to raise ab initio. We believe that section 405 calls for this result and that no constitutional principles or public policy require us to construe it otherwise. 387 F.2d at 506.

We respectfully submit that this reasoning is equally applicable here, and that petitioner's claim that the Commission has no jurisdiction over its system, like its other arguments, cannot be considered now.

The only question the Commission passed on in this case was whether a partial waiver of the non-duplication rule should be granted. The Commission held in essence that the circumstances offered in justification for a waiver, arising from the fact that the systems and the distant stations were located in different time zones, were among the very things which had led to the adoption of the rule. Thus, rather than affording grounds for a waiver, the time zone differential was a classic case for the application of the rule.[5/] This conclusion has not been challenged in this appeal.

The remaining sections of this brief deal *seriatim* with the issues presented by petitioner. They need be considered only if the Court is of the view that these issues are properly raised at this tim

5/ At issue in the rule making was whether the non-duplication provision should apply for an extended period, e.g., 15 days before and after the local broadcast, to simultaneous broadcasts only, or to some intermediate period. The Commission concluded that the 15 day period would be too disruptive of listening habits but that simultaneous non-duplication would not protect stations confronted with a "time zone differential problem." By extending the non-duplication period over a whole day, however, the Commission found that the disruption would be minimized throughout the country as a whole, and at the same time such protection would be sufficient to "preclude a CATV system, which brings programs across either border of the mountain time zone, from duplicating most, if not all, of a local station's network programs an hour or two before or after they are presented locally." *Second Report and Order*, 2 F.C.C. 2d 725, 749 (1966).

II. THE COMMISSION HAS THE AUTHORITY TO REQUIRE PETITIONER'S CATV SYSTEM TO DELETE PROGRAMS BROUGHT IN FROM DISTANT STATIONS ON THE SAME DAY THAT THESE PROGRAMS ARE BEING CARRIED OVER LOCAL STATIONS.

Petitioner's argument that the Commission lacks the authority to impose a non-duplication requirement is twofold. It asserts (Br. pp. 27-43) that the Communications Act provides no basis for regulating CATV systems directly. And in a separate argument (Br. pp. 10-27) it contends that although its system received distant signals via Commission licensed microwave facilities, the Commission may not impose conditions on those licenses with respect to non-duplication because this is simply an attempt to accomplish indirectly what the statutory scheme prevents it from doing directly.

In Southwestern Cable Co. v. U. S., 378 F.2d 118, this Court held that the Commission's authority may be "exercised only against licensees or applicants." Since CATVs fall in neither category, the Court therefore set aside a Commission order limiting the expansion of CATV systems in San Diego pending a hearing before the agency. 5/ The Supreme Court granted the Government's petition for writ of certiorari and the case has been briefed and argued. The major issue is that of the Commission's jurisdiction over CATV systems

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5/ But see Buckeve Cablevision, Inc. v. F.C.C., 387 F.2d 220 (C.A.D.C. 1967), where it was held that CATV "as a form of wire communication which enlarges the signal range of licensee stations to the potential detriment of the entire regulatory scheme" is subject to Commission authority.

not served by microwave radio facilities, and it is anticipated that a decision will be forthcoming during this term of Court. A decision upholding the Commission's jurisdiction would be dispositive of the contentions raised by petitioner here. On the other hand a holding adverse to the Commission would not necessarily affect the agency's power to adopt rules applicable to the microwave radio services, including those upon which CATV systems such as petitioner's depend, since these were not within the scope of this Court's Southwestern decision. Accordingly in this brief we address ourselves only to petitioner's contention that it is beyond the Commission's authority to require microwave-fed CATV systems to afford non-duplication protection.[7]

In our view this question was squarely and properly decided in Carter Mountain Transmission Corp. v. F.C.C., 321 F.2d 359 (C.A.D.C. 1963), cert. den. 375 U.S. 951 (1963). That case involved an application by a microwave common carrier for permission to construct facilities that were to be used to bring distant television signals to CATV systems located in several Wyoming communities. The authorization sought was in all material respects the same as that required by petitioner's affiliated carrier here. On appeal it was argued that the Commission erred in considering the economic impact that a grant of the microwave application would have on the local

7/ This requirement is specified in Section 21.712 of the Commission's rules, 47 C.F.R. 21.712. The rule is set forth in petitioner's Appendix, p. 86A-91A.

station by virtue of the new service the CATV systems would be in a position to provide. The Court ruled that the Commission's various communications responsibilities are not compartmentalized and that its decisions in one field must take into account its responsibilities in others. "It necessarily follows," the Court stated, "that in determining whether the authorization requested by appellant would be in the public interest the Commission was entitled -- if indeed it was not obliged -- to consider the use to which the facilities and frequencies requested were to be put, and to weigh that use as against other legally relevant factors, including the effect on existing local stations." 321 F.2d at 363. See also Idaho Microwave, Inc. v. F.C.C., 352 F.2d 729 (C.A.D.C. 1965).

The soundness of this holding is manifest. The Commission is charged by the Communications Act with regulation of common carriers and broadcast services in the overall public interest. Petitioner's argument (Br. 10-27) would negate the purpose of the Communications Act to achieve a comprehensive and coordinated regulation of all interstate communication by wire and radio through the Commission and to insure the "maximum benefits of radio to all the people of the United States." Sections 1, 307(b) of the Communications Act, 47 U.S.C. 151, 307(b); National Broadcasting Co. v. United States, 319 U.S. 190, 210-217; Federal Radio Commission v. Nelson Bros. Co., 289 U.S. 266, 279, 285.

A common carrier cannot construct a new facility or extend its existing facilities sua sponte or upon customer demand. The Communications Act gives the Commission jurisdiction of "every common carrier engaged in interstate or foreign communication by wire or radio," 47 U.S.C. §201. The Act also requires a license for all uses of radio, including its use for common carrier purposes, which can be obtained only upon a showing that the "public interest, convenience, and necessity" will be served 47 U.S.C. §301, §§307-310. In passing upon an application for a new broadcast authorization, the Commission must consider a resulting loss of existing broadcast service as a factor bearing upon the public interest. F.C.C. v. Sanders Bros. Radio Station, 309 U.S. 470, 475-476; Carroll Broadcasting Co. v. F.C.C., 258 F.2d 440, 443-444 (C.A.D.C.). Similarly, in the common carrier field, the competitive impact of a proposed facility upon existing common carrier service has been held to be a "relevant factor in weighing the public interest." F.C.C. v. R.C.A. Communications, Inc., 346 U.S. 86, 94.

Under the circumstances outlined in our counterstatement, pp. 1-3, supra, it was clearly proper for the Commission to consider the effect of the proposed common carrier operations upon the existing broadcast service in Great Falls, Montana. The relation of the two services is immediate and direct. Great Falls proposes to pick up signals broadcast by television stations in distant areas, transmit them by microwave to its CATV systems in the area served by local

television service, and thus deliver in practical effect competing television material. Following a comprehensive rulemaking proceeding the Commission concluded that unless some degree of protection, in the form of the non-duplication requirement, were established, the viability of local stations would be jeopardized to the detriment of the public interest in "the larger and more effective use of radio," 47 U.S.C. 303(g). See also 47 U.S.C. 301, 307(b). Though the rule it adopted may apply directly to the radio common carriers and only indirectly to the CATV system, it is not thereby rendered invalid.[8/]

8/ Petitioner's argument (Br. 21-27) that the Commission exceeded its authority when it considered the use to be made of the proposed common carrier service cannot be distinguished in substance from the position unsuccessfully urged by the carrier in Federal Power Commission v. Transcontinental Gas Pipe Line Corp., 365 U.S. 1. In Transcontinental the Supreme Court sustained the authority of the Power Commission to deny a certificate for the transportation of natural gas where the proposed end use--burning the gas under the purchaser's industrial boilers--was deemed inferior to other possible uses, although the Power Commission had no jurisdiction over direct sales for use by the purchaser. The authority of the Communications Commission to consider the proposed "end use" here would thus appear to be clearly established since, unlike the Natural Gas Act (see 365 U.S. at 8, 19), the Communications Act is intended to provide a comprehensive scheme of federal regulation of interstate communications. See Section 1, 47 U.S.C. §151. Community antenna television systems present an "end use" peculiarly related to television broadcasting. Clarksburg Publishing Co. v. F.C.C., 225 F.2d 511, 517 (C.A.D.C.).

III. THE NONDUPLICATION RULE DOES NOT UNCONSTITUTIONALLY RESTRICT PETITIONER'S RIGHT OF FREE SPEECH.

Great Falls argues (Br. 44-49) that the CATV rules infringe upon its right of free speech in contravention of the Communications Act, and the First Amendment of the Constitution. Its argument is premised on the ground that the nonduplication rule inhibits the distribution of Constitutionally protected material. We believe it is clear that no such violation exists. In National Broadcasting Co. v. United States, 319 U.S. 192 (1943), the Supreme Court made clear that reasonable regulation of the use of the radio spectrum in the interest of the general public is not a violation of the First Amendment. See also California Citizens Band Association v. United States, 375 F.2d 43, 55 (C.A. 9, 1967); Lafayette Radio Electronics Corp. v. United States, 345 F.2d 278 (C.A. 2, 1965). In NBC the Court concluded (319 U.S. at 227):

> * * * The right of free speech does not include however, the right to use the facilities of radio without a license. The licensing system established by Congress in the Communications Act of 1934 was a proper exercise of its power over commerce. The standard it provided for the licensing of stations was the "public interest, convenience, or necessity." Denial of a station license on that ground, if valid under the Act, is not a denial of free speech.

If, as we urge, the Commission has been granted the authority by Congress to limit the duplication of local television signals through the importation of distant signals, the NBC case, supra, makes clear that such a limitation raises no substantial free speech question. CATV systems constitute a part of the scheme of television distribution, which unlike other modes of expression, make use of

made signals as a sine qua non of their operation. Thus in essence the CATV regulations, like the network rules at issue in the NBC case, are another aspect of regulation of the use of the airwaves.

The Commission's effort to preserve local television by regulating CATVs has the same constitutional status under the First Amendment as regulation of the transmission of signals by the originating television stations. The crucial consideration is that they use radio signals and that they have a direct impact upon, and relationship with, the television broadcast service. Indiscriminate CATV development, feeding upon the broadcast service, is capable of destroying large parts of it. The public interest in preventing such a development is manifest.

With respect to the regulation of [illegible], the courts have consistently upheld its validity against challenges that First Amendment rights were being infringed. In the Carter Mountain case the court rejected the argument that nonduplication requirements constituted an improper restraint on free speech, stating that "protection of the public interest does not amount to 'censorship,'" 321 F.2d at 364. Similarly in Buckeye Cablevision Co. v. F.C.C., 387 F.2d at 225, the court observed:

> It is true that CATV systems disseminate programs carrying a wide range of information. But we think the restraint imposed by the Rules is not more than is reasonably required to effectuate the public interest requirements of the Act.

See also Idaho Microwave, Inc. v. F.C.C., 352 F.2d at 729, 733 (C.A.D.C.); and Conley Electronics Corporation v. U. S., ___ F.2d ___, decided April 22, 1968 (C.A. 10).

In sum, the regulation of the airwaves is an exercise of the commerce power. Federal Radio Commission v. Nelson Brothers Bond & Mortgage Co., 289 U.S. 266, 279 (1933), and Congress may subject their use to reasonable regulation in the public interest, whether the use of radio signals be made by radio and television stations or by CATV systems. Such regulation which, as we have shown above, is reasonably related to valid objectives, is not an infringement upon the rights of free speech of either the CATV system operator or the viewing public.

IV. THE COMMISSION'S NONDUPLICATION RULE STRIKES A FAIR BALANCE BETWEEN COMPETING INTERESTS, AND PROTECTS THE PARAMOUNT PUBLIC INTEREST.

Petitioner challenges the wisdom of the nonduplication rule on the ground that it unfairly restricts competition between local television stations and CATV (Br. 63-78). This matter was, of course, fully considered in the rule making proceeding, where the Commission concluded that, on the contrary, the nonduplication rule corrects a competitive situation that is basically unfair. Thus, the Commission explained that local television stations like those in Great Falls

> . . . obtain their programs, for the most part, from various program suppliers. The most important of these, for most stations, are the national television networks. However, stations deal in addition with the distributors of feature film, cartoon, syndicated, and sports programming. The station obtains the right to exhibit network programs by offering to the network attractive

> audience circulation, etc., and by giving up to the network a major portion of the compensation which the sponsor or participating advertiser pays for the use of the station's facilities in connection with that program. The station normally obtains the right to exhibit nonnetwork programs by outright payments to nonnetwork program suppliers. 38 F.C.C. at 703, par. 52.

On the other hand, a CATV system, like petitioner's, is not faced with these expenses because it

> . . . presently stands outside of the program distribution process we have described. It has not been found subject to the requirements of section 325. [47 U.S.C. 325 forbids broadcast stations from rebroadcasting without consent programs of other stations. There is no such statutory restriction applicable to CATVs.] It does not compete for network affiliation, nor for access to syndicated programs, feature films, or sports events. It is not concerned with bidding against competing broadcasters for the right to exhibit those programs nor with bargaining with program suppliers for time and territorial exclusivity. 38 F.C.C. at 704, par. 54.

See also the Commission discussion in <u>Second Report and Order</u>, 2 F.C.C. 2d at 778, pars. 132-133.

An avowed purpose of the nonduplication rule is to redress this imbalance so as to enhance the ability of the local station to survive. We emphasize that contrary to petitioner's assertions, this is not a finding of unfair competition as that concept is embodied in the Federal Trade Commission Act. Nor does the rule purport to create property rights in programming or in any way to

implement the Copyright Act. See First Report, 38 F.C.C. at 740. Rather, it is a rule reflecting a policy designed to further the "public interest in the larger and more effective use of radio" (Section 303(g) of the Communications Act of 1934, as amended, 47 U.S.C. 303(g)), by integrating CATV into the nationwide television system in a fair and orderly manner--in a way which permits CATV to discharge its valuable function of bringing needed supplementary services, without being destructive of the more important local service and indeed of the parent broadcast service.

Nor is their substance to petitioner's claim that the rule is at odds with a national policy of free competition in the broadcast field. Indeed the case on which it chiefly relies makes clear that where competition may be harmful to the public interest, it is an element which the Commission must take into account. F.C.C. v. Sanders Bros Radio Station, 309 U.S. 470. Though petitioner quotes extensively from this opinion, it has seen fit to omit the following passage:

> This is not to say that the question of competition between a proposed station and one operating under an existing license is to be entirely disregarded by the Commission and, indeed, the Commission's practice shows that it does not disregard that question. It may have a vital and important bearing upon the ability of the applicant adequately to serve his public; it may indicate that both stations--the existing and the proposed--will go under, with the result that a portion of the listening public will be left without adequate service; it may indicate that, by a division of the field, both stations will be compelled to render inadequate service.

See also Carroll Broadcasting Co. v. F.C.C., 258 F.2d 440 (C.A.D.C. 1958). And in Carter Mountain, supra, the court held that the Commission was "fully warranted" in imposing nonduplication conditions on the CATVs.[9/]

Finally, in a case identical to this one in all material respects, the Fourth Circuit upheld the nonduplication rule as "seemingly . . . a fair adjustment and accommodation of conflicting claims." Wheeling Antenna Co., Inc. v. U.S. and F.C.C., ___ F.2d ___. The following from that opinion is equally applicable to the case at bar:

> For its survival, of course, a station needs financial support. Commercial advertisements are a chief source and these are attracted by the number of a station's viewers, for they are the advertisers' prospective customers. Consequently, to insure its permanence a station is entitled to some protection against dilution of its coverage through CATV's introduction of the same programs from more removed stations. In weighing the hurt to CATV against the help to TV, there are several considerations besides the hope of preserving the station as a local and national asset. One is the fact that the local station is put to substantial expense in procuring programs, while CATV has so far been able to use them without sharing this burden.
>
> On balance, we cannot say the Commission has not been impartial in fulfilling its obligations. Neither the rules nor their administration are shown to be unjust, including the particular rule now in suit. Seemingly, it represents a fair adjustment and accommodation of conflicting claims to first place in the public interest. Cf. Channel 9 Syracuse, Inc. v. FCC, supra, 385 F2d 969, 971, and Carter Mountain Transmission Corp. v. FCC supra, 321 F2d 359, 363, cert. den., 375 US 951. The Commission's order is an evenhanded and justified execution of this policy . . . (Footnote omitted.)

9/ In Conley Electronics, supra, the Court stated "Indeed, we think the rule is not only consistent with Sanders, but affirmatively implements it. . . We hold that the non-duplication rule was a reasonable exercise of the Commission's authority.

V. THE COMMISSION WAS NOT REQUIRED TO HOLD A HEARING ON PETITIONER'S REQUEST THAT IT BE EXEMPTED FROM THE NON-DUPLICATION RULE.

Petitioner argues (Br. 49-63) that the relevant statute and regulations, as well as due process required a hearing before its long standing business practices are modified. 10/ Dealing with precisely the same kind of claim the Fourth Circuit in the Wheeling case, supra, stated:

> At its option the Commission may, as it did here, adjudicate by reference to a pertinent general rule. Cf. Securities Comm'n v. Chenery Corp., 332 US 194, 203 (1947). In the present circumstances no hearing was demandable. FPC v. Texaco Inc., 377 US 33, 44 (1964); United States v. Storer Broadcasting Co., 351 US 192, 205 (1956). Otherwise, the Commission would be intolerably and impractically embroiled in a multiplicity of trials. This does not mean, of course, that a petitioner goes unheard. It means only that the Commission may make its judgment on the petitioner's papers. The decision then becomes reviewable in whatever manner the statute may permit.

And in Conley Electronics Corporation v. U. S., supra, the Tenth Circuit reached the same result under identical circumstances.

10/ The order in this case is not as petitioner suggests a revocation order under 47 U.S.C. 312. Pursuant to that section, the Commission may issue such orders to any person failing "to observe any rule or regulation of the Commission" authorized under the Act. They may be entered only after a hearing in which the person involved has been afforded an opportunity to show cause why the order should not be issued. And the proceedings are reviewable only in the Court of Appeals for the District of Columbia Circuit, 47 U.S.C. 402(b)(7).

Here the Commission's order simply denied a waiver of one of its rules applicable to all CATV systems. The nonduplication rule generally becomes operative when the local station requests program exclusivity protection from the CATV operator. However, upon receipt of this request, the CATV system may petition the Commission to waive the rule. A petition for waiver operates to stay compliance pending a determination of the merits of the waiver petition. Hence, the necessity for including a clause fixing the date for compliance in any order denying a petition for waiver.

This reasoning is supported not only by the Supreme Court cases cited, but also by the Court's opinion in California Citizens Band Association v. U.S., 375 F.2d 43, 51-52 (C.A. 9, 1967), cert. denied __ U.S. __. See also American Airlines v. Civil Aeronautics Board, 359 F.2d 624 (D.C. Cir., 1966), cert. denied, 385 U.S. 843; Airline Pilots Association, International v. Quesada, 276 F.2d 892 (C.A. 2, 1960). All of these authorities establish that where general rules are adopted, which apply to all coming within their terms, individual adjudicatory hearings are not required before the rules may become effective.

The justification for proceeding without a hearing is far stronger here than in any of the above cases. There appears to be no material facts in issue at all. The grounds asserted for a waiver, the choice of programs made possible by the time zone differential, far from being a reason to depart from the rule, is one of the very situations the rule was designed to meet. And finally no hearing was ever requested by the petitioner. The record below is thus devoid of any statement by the petitioner as to what it would show in such a proceeding.

In the Storer case, cited above, the Supreme Court observed: "We do not think Congress intended the Commission to waste time on applications that do not state a valid basis for a hearing." 351 U.S. at 205. Clearly this is the case here.

CONCLUSION

For the reasons stated, the Commission's action should be affirmed.

Respectfully submitted,

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Washington, D. C. 20530

Federal Communications Commission
Washington, D. C. 20554

April 29, 1968

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ Joseph A. Marino

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

WAIIAN PARADISE PARK CORPORATION, Hawaii corporation, Appellant,	)	
vs.	)	NO. 22394
IENDLY BROADCASTING CO., INC., Ohio corporation, Appellee.	)	

On Appeal from the United States District Court
for the District of Hawaii

APPELLEE'S ANSWERING BRIEF

FILED

AUG 15 1968

WM. B. LUCK, CLERK

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IN THE UNITED STATES COURT OF APPEALS

NINTH CIRCUIT

WAIIAN PARADISE PARK CORPORATION) awaii corporation,)		
Appellant,)		
vs.)		NO. 22394
IENDLY BROADCASTING CO.,) Ohio corporation,)		
Appellee.)		

APPELLEE'S ANSWERING BRIEF

STATEMENT OF JURISDICTION

The jurisdiction of the District Court was based upon 28 USC §1332. e jurisdiction of this Court rests on 28 USC §1291. A final judgment s entered and filed in the District Court on September 19, 1967 (R-152). ice of Appeal was filed by Appellant on October 19, 1967 (R-174).

FRIENDLY'S EVIDENCE IN SUPPORT OF THE FINDINGS OF FACT DESIGNATED AS HAWAIIAN'S SPECIFICATION OF ERRORS

Hawaiian has specified certain findings of fact as error; however, as not argued all such specifications. Friendly will, therefore, nt out affirmative support for the specifications argued; namely, cification of errors 1, 4 and 7.

Specification number one contains three parts. Friendly's evidence support of the finding of fact designated as the first part, that "The

December 16, 1966 (Ex. P-6), he had express authority from Hawaiian do so," is found in the testimony of both Mr. Becker and Mr. Watumull. . Becker's testimony is found on pages 216 through 218, 223 through), 232, 234 through 239, 244, 245, 249, 252 through 254 and 256 through) of the transcript. Mr. Watumull's testimony is found on pages 277, ;, 301, 326, 329, 331 through 334, 353 and 354 of the transcript.

Friendly's evidence in support of the second part of specification nber one, "that he [Mr. Becker] had good reason to believe that he l authority to do so [sign the letter of December 16, 1966] on behalf Hawaiian," is as follows:

a) Exhibits D-1, P-2F, P-3 through P-6, P-9, P-12 and P-12A;

b) All of the testimony pointed out above regarding part one of specification number one.

c) Additional testimony of Mr. Becker found on pages 196 through 210 of the transcript;

d) Additional testimony of Mr. Watumull found on pages 268, 269, 271 through 273, 303 through 308, and 321 through 320 of the transcript; and

e) The evidence which supports the apparently uncontested findings of fact numbered 9, 10, 11, 14 through 23, 29, 30, 32, 37, 38 and 41 and found in the record on pages 114 through 121.

Friendly's evidence in support of the third part of specification

mber one, "that Hawaiian was agreeable to the kind of agreement he

r. Becker] was signing," is as follows:

a) All of the testimony pointed out above regarding part one of specification number one;

b) The additional testimony of Mr. Becker found on pages 240 through 242 of the transcript;

c) The additional testimony of Mr. Watumull found on pages 321, 322, 330, and 335 through 338 of the transcript; and

d) Exhibits P-12 and D-7.

Friendly's evidence in support of the finding of fact designated

specification of error number four is as follows:

a) The testimony of Mr. Becker found on pages 196 through 218, 223 through 229, 255, and 256 of the transcript;

b) The testimony of Mr. Dobin found on pages 45 through 52, 59, 60, 62 through 64, 66 through 80, 83, 92 through 94, 104, 124 through 134 and 152 through 158 of the transcript;

c) The testimony of Mr. Watumull found on pages 268, 269, 271 through 273, 277, 286, 301, 303 through 308, 321 through 320, 329, 331 through 334, 353 and 354 of the transcript; and

d) Exhibits D-1, P-2F, P-3, P-4, P-6, P-12, and P-12A.

Friendly's evidence in support of the finding of fact designated as ecification of error number seven is as follows:

a) Exhibits P-1, and P-2A through P-2G;

b) The testimony of Mr. Courtney on pages 11, and 14 through 16 of the transcript;

c) The testimony of Mr. Dobin on pages 36 and 37 of the transcript; and

d) The testimony of Mr. Becker on pages 190 and 191 of the transcript.

QUESTIONS PRESENTED

1. Was there sufficient evidence for the District Court to hold that the time Mr. Becker signed the letter of December 16, 1966 (Ex. P-6), had express authority from Hawaiian to do so?

2. Was there sufficient evidence for the District Court to hold that . Becker had good reason to believe that he had the authority to sign December 16, 1966 letter (Ex. P-6) on behalf of his client?

3. Was there sufficient evidence for the District Court to hold that . Dobin had the right to believe that Mr. Becker had the authority to n the December 16, 1966 letter agreement (Ex. P-6).

4. Did the District Court err in denying Hawaiian's Motion for der Vacating Injunction and Dismissing Action filed on September 18, 67 (R-144)?

5. Was there sufficient evidence for the District Court to hold

t station KTRG-TV (Channel 13) is one of but four commercial tele-ion stations in Honolulu and the F.C.C. certificate or license or permit operate said station is a unique chattel or asset; that the other assets chattels or property which Hawaiian contracted to sell Friendly, ile not unique unto themselves, are flavored or tainted by the F.C.C. erating permit; and that the basic agreement, as amended, is oject to specific performance?

6. Has Hawaiian, by its conduct since the final judgment entered the District Court on September 19, 1967 (R-152), waived its right an appeal?

SUMMARY OF ARGUMENT

The evidence supports the conclusion that Mr. Becker had express hority, implied authority and apparent authority to enter into the letter eement of December 16, 1966.

Hawaiian's F. C. C. operating license is a unique chattel and an eement to assign such license is specifically enforceable.

It would be unreasonable to read the December 16, 1966 letter in a nner that would allow Hawaiian to terminate the basic agreement when erything therein contemplates consummation of the transfer once F. C. C. proval is granted.

Hawaiian has waived its right of appeal by its actions since the final lgment was filed herein on September 19, 1967.

ARGUMENT

I. MR. BECKER HAD THE AUTHORITY TO BIND HAWAIIAN TO
IE LETTER AGREEMENT OF DECEMBER 16, 1966.

Friendly has maintained throughout these proceedings that the
ter agreement of December 16, 1966 (Ex. P-6) is binding on Hawaiian.
e evidence adduced at the trial supports the District Court's findings
express authority, implied authority, and apparent authority on the
rt of Hawaiian's Washington, D. C. attorney, Mr. Becker, to enter
o and sign the December 16, 1966 letter. The letter is binding on
waiian if Mr. Becker had either express, implied or apparent
thority to act on behalf of his client.

EXPRESS AUTHORITY

Express authority is defined in Black, Law Dictionary (4th ed. 1957)
page 691 as "Authority delegated to agent by words which expressly
thorize him to do a delegable act. Authority distinctly, plainly expressed,
ally or in writing. Authority which is directly granted to or conferred
on agent in express terms. [Citations omitted.]" Mechum, Agency
l (4th ed.) states: "Express authority requires little definition. As
e name suggests, it means that it can be proved that the principal in
press and explicit language made clear to the agent his willingness or
sire that the act in question be done."

Whether Mr. Becker had express authority to enter into the letter
reement of December 16, 1966 is a question of fact. The trier of

:t, after listening to all the witnesses and reviewing all the exhibits, s found that "At the time Mr. Becker signed the letter of December 16, 66 (Exhibit P-6), he had express authority from Defendant to do so." here is much testimony supporting this finding of fact and the transcript ferences have been listed above in Friendly's designation of evidence support of the finding of fact listed by Hawaiian as part one of speci- :ation of error number one.

In addition to the direct evidence on express authority, there was idence that showed Hawaiian was aware of and accepted the benefits the December 16, 1966 letter and from which the trial judge could asonably infer Hawaiian's knowledge of the agreement. For example:

1. Hawaiian's attorney was present at all of the F. C. C. hearings (T-87) which Hawaiian knew could not be completed and a decision rendered before February 3, 1967 (T-245);

2. Two of Hawaiian's employees, Mr. Lindemann and Mr. Tateishi, went to Washington, D. C. and testified before the hearing examiner (T-86, 8 of 356 and 357);

3. Even after the termination date of February 3, 1967 set forth in the basic agreement, Hawaiian participated in the preparation and filing of proposed findings of fact and conclusions of law and replys to the Broadcast Bureau's proposed findings of fact and conclusions of law (T-89 through 91);

4. Hawaiian did not send its termination letter until approximately ten weeks after February 3, 1967 (Ex. P-10);

5. Hawaiian's home office had knowledge of the status of the F. C. C. proceedings (Ex. 11A - F; T-355);

6. Hawaiian did not attempt to terminate the agreement with Friendly until it had reached an agreement on the purchase price of $660, 000 for the television station with Bishop Industries, $110, 000 more than the contracted price with Friendly (T-321 and 342); and

7. Hawaiian has made no attempt to return to Friendly the $5, 000 attorney's fees paid to Mr. Becker pursuant to the December 16, 1966 letter agreement (T-337).

IMPLIED AUTHORITY

Implied authority is defined in Black, Law Dictionary (4th ed. 1957) page 169 as "Actual authority circumstantially proved. That which the incipal intends his agent to possess, and which is implied from the incipal's conduct. It includes only such acts as are incident and cessary to the exercise of the authority expressly granted. [Citations nitted.]"

In Moore v. Switzer, 78 Colo. 63, 239 P. 874, it is stated at ge 65 as follows:

> . . . Implied authority of an agent is actual authority evidenced by conduct, that is, the conduct of the principal has been such as to justify the jury in finding that the agent had actual authority to do what he did. This may be proved by evidence of acquiescence with knowledge of the agent's

acts, and such knowledge and acquiescence may be shown by evidence of the agent's course of dealing for so long a time that knowledge and acquiescence may be presumed. . . .

Mechum, Agency §54 (3) (4th ed.) states that the most common stance of this type of authority is found in cases where the agent has peatedly exercised some power not expressly given him and the incipal, with knowledge of the same, has, by making no objection, citly sanctioned the continuation of the practice. There is no doubt at the practice indulged by Hawaiian and its Washington, D. C. attorney s neatly into this statement of the law.

The trial judge has found that Mr. Becker had good reason to lieve he had the authority to sign the letter of December 16, 1966 on half of Hawaiian. The trial judge had every right to make this finding sed upon the past actions of Hawaiian (Ex. P-2G, P-3, P-4, and P-12A), d the procedure established by Hawaiian allowing Mr. Becker to negotiate its behalf (T-326 and 329). Additional evidence in this regard is set rth above in Friendly's designation of evidence in support of the finding fact listed by Hawaiian as part two of specification of error number one.

APPARENT AUTHORITY

The basis for apparent authority has been well stated in 3 Am. Jur. 2d, ency, §73 at pages 475 and 476 as follows:

The liability of the principal for the acts and contracts of his agent is not limited to such acts and contracts of the agent

as are expressly authorized, necessarily implied from express authority, or otherwise actually conferred by implication from the acts and conduct of the principal. So far as concerns a third person dealing with an agent, the agent's 'scope of authority' includes not only the actual authorization conferred upon the agent by the principal, but also that which has apparently been delegated to him. Apparent authority, or ostensible authority, as it is also called, is that which, though not actually granted, the principal knowingly permits the agent to exercise, or which he holds himself out as possessing. In effect, therefore, an agent's apparent authority is, as to third persons dealing in good faith with the subject of his agency and entitled to rely upon such appearance, his real authority, and it may apply to a single transaction, or to a series of transactions. [Emphasis supplied.]

And in §74 at page 476 and 477, it is stated, in part, as follows:

. . . The apparent authority of an agent results from statements, conduct, lack of ordinary care, or other manifestations of the principal's consent, whereby third persons are justified in believing that the agent is acting within his authority . . . .

Apparent authority may be, and often is, derived from a course of dealing or from the fact that a number of acts similar to the one in question were assented to, ratified, or not disavowed by the principal. The acquiescence of the principal in an extension of his authority by an agent in the transaction in question may be

sufficient to create the appearance of authority in the agent to do such act; the acquiescence in, and the consequent scope of, such authority, is to be determined not only by what the principal actually does know of the acts of the agent within the employment, but also as to what he should, in the exercise of ordinary care and prudence, know the agent is doing in the agency transaction. In such case, the appearance of authority is created because of the fact that the third person is entitled to assume that the principal is cognizant of the exercise of authority and would forbid it if it were unauthorized.

Stated inclusively, then, the rule is that if a principal acts or conducts his business, either intentionally or through negligence, or fails to disapprove of theagent's act or course of action so as to lead the public to believe that his agent possesses authority to act or contract in the name of the principal, such principal is bound by the acts of the agent within the scope of his apparent authority as to any person who, upon the faith of such holding out, believes, and has reasonable ground to believe, that the agent has such authority, and in good faith deals with him [Emphasis supplied.]

In T. G. Bush Grocery Co. v. Conely, 61 Fla. 131, 55 So. 867, aintiff was a wholesale grocer and Defendant was a retail dealer. Parker as a traveling salesman for Plaintiff whose authority was to sell goods at ices as instructed by Plaintiff. Plaintiff admitted that while Parker d no specific authority to collect money for goods sold, yet he did llect and Plaintiff did not object to it and that Plaintiff recognized his

thority to collect money by not objecting to the practice.

Parker was not authorized to give rebates on the bills for ods sold and Plaintiff had no knowledge that he was allowing rebates Defendant. Plaintiff sued to get rebates which Parker had allowed efendant. The Court stated at page 135:

> Where a principal has, by his voluntary act, placed an agent in such a situation that a person of ordinary prudence, conversant with business usages and the nature of the particular business, is justified in presuming that such agent has authority to perform a particular act, and therefore deals with the agent, the principal is estopped, as against such third person, from denying the agent's authority. [Citation omitted.] Whether or not an act is within the scope of an agent's apparent authority is to be determined, under the foregoing rule, as a question of fact, from all circumstances of the transaction and the business. Where one of two persons must suffer for the wrongful act of a third, he who gave the power to do the wrong must bear the burden of the consequences. [Citations omitted.]
>
> If one holds another out to the world and accredits him as his agent, he is bound by that person's acts done within the scope of the agency thus given to him. In such cases the question is, not what authority was intended to be given to the agent, but what authority was the third person dealing

with him justified from the acts of the principal in believing was given to him. [Citations omitted.]

In the case now before this Court, Plaintiff's witnesses testified at after Mr. Becker communicated Defendant's rejection of the vember supplement to agreement to Mr. Dobin, a new arrangement s agreed upon, communicated to and accepted by Mr. Watumull, and r. Watumull's acceptance communicated to Mr. Dobin (T-224 through 8). In International Union of Op. Eng., Local 406 v. Guy Scroggins, c., (Ct. of Appeals La.) 168 So. 2d 724, the union sought an injunction prevent violation of terms of a contract between the union and Defendant. idence showed the union asked the construction superintendent on the to sign a collective bargaining agreement which he refused to do. He id he would talk about the contract with the corporate president and ajor stockholder. After talking to the corporate president and major ockholder, he signed the contract. The Court held that after talking th the corporate president and major stockholder he had apparent thority to sign the contract and that the employer was estopped to deny s agency or his authority to so sign. The Court also found that the perintendent had no actual authority but he did possess apparent thority.

An agent's course of conduct, apparently acquiesed in by his nployer, was sufficient to show apparent authority in Shaw v. Bailey, t. of Appeals Ala.) 55 So. 2d 132, which was an action in detinue to cover a car sold to Defendants by Miles, an employee of Plaintiff

ho worked in Plaintiff's body shop, but not as a salesman at Plaintiff's ed car lot. It was conceded Miles had no express authority to sell rs.

Right after being fired by Plaintiff, Miles went to Plaintiff's used r lot and took a car, saying that he was taking it to the shop for repairs. iles took the car to Defendants and sold it for $275, $5 cash and a check r $270 made payable to Miles as representative of Plaintiff. Miles gave efendants a bill of sale executed before a notary public and signed Hubert A. Miles, Rep. Kelly Shaw Motor Co."

During the trial Defendants showed that Miles had printed cards owing he was a salesman for Plaintiff; that Defendants had previously ught a car from Miles as a salesman for S&S Motor Co., of which aintiff was a partner; and that Miles had sold or attempted to sell rs from Plaintiff's company to others. It was held that Defendants owed that Miles had apparent authority to sell the subject car and at Plaintiff was estopped to deny such authority.

In a case in which Plaintiff sought to recover from Defendant oney loaned to its agent on his representation that the Defendant would ld the money and pay interest until enough was accumulated to buy an nuity, Mattice v. Equitable Life Assur. Soc., 170 Wis. 504, 71 N.W. 262, the Court found that the agent, who used the money for his own nefit, had no actual authority to borrow the money and had not pre- ously borrowed money on Defendant's name. After stating that parent authority must be traced to the principal, the Court said that

ree elements are necessary to establish apparent authority: "(1) Acts one by the agent or principal justifying belief in the agency. (2) Knowledge the party thereof sought to be held (in the present case, appellant).) Reliance thereon by the plaintiff, consistent with ordinary care and rudence." The Wisconsin Supreme Court also stated that the rule that a erson dealing with an agent known to be acting for a principal must at s peril ascertain the extent of the agent's authority must be read in onnection with the rule that if a third person, because of appearances r which the principal was responsible, believes and has reasonable round to believe that the agent possessed power to act for the principal the particular transaction, if such third person was, in the exercise reasonable prudence, justified in believing that the agent possessed e necessary authority, then the principal is responsible to third person e same as if the agent possessed all the power he assumed to possess.

During the course of the trial, it was brought out that because the distance separating the parties and F. C. C. rules, it was necessary r the parties to be represented by counsel. Also, both parties are orporations and must, therefore, act through their agents. In Brace v. orthern Pacific R. Co., 63 Wash. 417, 115 P. 841, the Court said that corporation, because of its very nature, must necessarily act through s agents; that persons are justified in relying upon the apparent authority such conceded agents; and that a corporation, being required to appoint agent having such apparent authority as to be able to mislead persons ealing with them, should be required to secure an agent who will not

ct in excess of his actual authority.

Another case along the same vein, General Motors Truck Co. s. Texas Supply Co., 64 F. 2d 527, in which Defendant's regional manager greed to buy back defective trucks sold to Plaintiff by an independent ealer, the Court held that the act of an agent within the apparent scope f his authority, though not within the scope of his real authority, is inding on the principal where a loss would otherwise result to one ho in good faith relied on such apparent authority. The Court also aid that an act was within the apparent scope of an agent's authority hen a reasonably prudent person, having knowledge of the usages of he business, would be justified in supposing that the agent was uthorized to perform the act from the character of his known duties.

Without doubt, the evidence in the case now before this Court, s brought out in the examinations of Mr. Dobin and Mr. Becker, nd even Mr. Watumull himself, clearly shows that the Defendant had lothed Mr. Becker with an abundance of apparent authority.

II. SPECIFIC PERFORMANCE OF A CONTRACT TO SELL A NIQUE CHATTEL.

The basic agreement (Ex. P-1) provided for a purchase price of 550,000 for all of the fixed and tangible assets of KTRG-TV (Channel 13) ncluding the F. C. C. operating license or permit. Mr. Courtney estinated the fixed assets to be worth $250,000 (T-11). This leaves a alue of $300,000 to be applied to the operating license. While the price

alloted to a chattel does not make it unique, it does indicate the value of the chattel in the eyes of the seller and buyer. Insofar as the KTRG-TV operating license is concerned, the price placed on it shows that the value of the operating license exceeds by $50,000 the value of all the other fixed assets of the station and, while not controlling, is indicative of the uniqueness of the operating license.

It is well established that equity will decree the delivery of specific unique chattels. See 81 C. J. S., Specific Performance, §67. It has been held in many jurisdictions that a contract to sell, transfer, or assign a liquor license is specifically enforceable. Ibid. It has also been held that contracts to assign Interstate Commerce Commission certificates of convenience and necessity are specifically enforceable, at least to the extent of compelling the parties to the agreement to take the steps necessary to effectuate such assignment. See 15 ALR 2d 893 where it is stated, in part, as follows:

> It appears that the fact that a transfer of a certificate of convenience and necessity generally requires the approval of the commission issuing such certificate does not preclude a court from decreeing specific performance of an agreement to transfer such a certificate at least to the extent of compelling the parties to the agreement to take the steps necessary to effectuate such transfer, such as applying to the commission for an approval of the transfer and furnishing any information or papers necessary on such application.

See also Watson Bros. Transp. Co. v. Jaffa (CA 8th Iowa) 143 F2d 340; Lennon v. Habit, 216 N. C. 141, 4 S. E. 2d 339; and Royal Coach Lines, Inc., 140 N. J. Eq. 19, 52 A. 2d 763, app. dismd 2 N. J. 3, 65 A. 2d 264.

The scarcity of a chattel is, of course, an important factor ecognized by courts of equity in determining whether specific performnce of a contract for its sale will be granted. Even Defendant concedes hat there are only four commercial television stations in Honolulu. 'urthermore, it is uncontroverted that under the present F. C. C. allotnent of channels no new channels can be acquired (T-11, 14 through 16, 6, 37, 190 and 191).

Plaintiff concedes that the fixed chattels of Defendants television tation are not unique chattels and would not be subject to specific erformance but for the F. C. C. operating license which is not only ne of but four such operating licenses allotted to Honolulu but which annot be duplicated at this time by the grant of an additional operating icense by the F. C. C.

III. THE TRIAL COURT DID NOT ERR IN APPLYING THE ETTER AGREEMENT OF DECEMBER 16, 1966.

On September 15, 1967, counsel for Hawaiian made an oral motion o vacate the preliminary injunction and to dismiss the action (T-408). On September 18, 1967, Hawaiian filed a written motion asking for the ame relief, together with a statement of reasons in support of the

notion. The Trial Court spoke at length on the reasons denying Hawaiian's motion (T-422 through 437, 440 and 441) and those reasons are incorporated herein by reference.

At one point (T-422), the Trial Court stated: "That December 16 etter must be read in connection with the entire record that is available, and that is proper to be constituted with it."

Hawaiian's counsel replied: "I concur, your Honor."

Obviously, if the December 16, 1966 letter is read with the basic agreement (Ex. P-6) and the letter agreement of January 11, 1966 changing the closing date (Ex. P-2G), the parties contemplated a closing of the deal within five days after final F. C. C. approval and urther intended and did bind each to the other to perform as stated in he basic agreement as amended. Any other interpretation renders the December 16, 1966 letter void and negates all of the efforts by Hawaiian and Friendly to get F. C. C. approval of the assignment of the operating icense. Surely neither party ever intended terminating the sales agreement after F. C. C. approval, and to allow Hawaiian to terminate after F. C. C. approval would result in a manifest injustice.

IV. HAWAIIAN HAS WAIVED ITS RIGHT TO BE HEARD ON APPEAL.

On January 8, 1968, Friendly filed a motion herein seeking to dismiss this appeal. The motion was accompanied by points and authorities n support of the motion as well as by affidavits and exhibits. On February 8, 1968, an order was issued herein denying the motion but

allowing Friendly to renew the motion when this cause is submitted on the merits.

Friendly hereby resubmits its said motion and incorporates herein by reference said motion with all of its supporting memorandum, affidavits and exhibits.

CONCLUSION

Based upon the reasons and authorities stated above and the record herein, it is respectively submitted that the Trial Court committed no error prejudicial to Hawaiian, made proper findings of fact in respect to the letter agreement of December 16, 1966 and properly concluded that the said letter agreement was binding on Hawaiian and that the basic agreement as amended was specifically enforceable.

It is further submitted that the judgment of the District Court should be affirmed and Appellee should have its costs incurred herein.

Dated at Honolulu, Hawaii, this 13th day of August, 1968.

Respectfully submitted,

William H. Dodd

WILLIAM H. DODD
Attorney for Appellee
Friendly Broadcasting Co., Inc.

Of Counsel
Fong, Miho, Choy & Robinson

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have amined Rules 18, 19 and 39 of the United States Court of Appeals for the nth Circuit, and that, in my opinion, the foregoing brief is in full comance with those rules.

William H. Dodd

WILLIAM H. DODD

No. 22394

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

HAWAIIAN PARADISE PARK CORPORATION, a Hawaii corporation,

Appellant,

vs.

FRIENDLY BROADCASTING CO., INC., an Ohio corporation,

Appellee.

On Appeal from the United States District Court for the District of Hawaii

APPELLANT'S OPENING BRIEF

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NINTH CIRCUIT

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APPELLANT'S OPENING BRIEF

STATEMENT OF JURISDICTION

This was an action between citizens of different states and the matter in controversy exceeded $10,000, exclusive of interest and costs (R. 3). The United States District Court for the District of Hawaii had jurisdiction of the cause of action under 28 U.S.C.A. §1332. This Court has jurisdiction to hear this appeal by virtue of 28 U.S.C.A. §1291. Appellant has taken this appeal under Rules 73 and 75 of the Federal Rules of Civil Procedure.

STATEMENT OF THE CASE

Pleadings:

On May 3, 1967, Friendly Broadcasting Co., Inc., an Ohio corporation, appellee herein and hereinafter referred to as "Friendly", brought suit against Hawaiian Paradise Park Corp., a Hawaii corporation, appellant herein and

hereinafter referred to as "Hawaiian". Friendly sought (1) to enjoin Hawaiian from withdrawing, terminating or in any manner whatsoever, interfering with Friendly's application to transfer Hawaiian's Federal Communications Commission (hereinafter referred to as "FCC") license to operate television station KTRG-TV (Channel 13) in Honolulu, Hawaii, or (2) without the recognition of Friendly's alleged prior rights, from selling, attempting to sell or negotiating for sale any and all of the property described in an agreement dated January 7, 1966 (Ex. P-1) until the time specified in a letter dated December 16, 1966 (Ex. P-6) had expired (R. 7). The agreement dated January 7, 1966 is hereinafter referred to as the "basic agreement". The letter dated December 16, 1966 is hereinafter referred to as the "December 16 letter".

Friendly amended its complaint to allege that Hawaiian's license to operate the television station, together with the other property to be transferred under the basic agreement, constituted a unique chattel and prayed that Hawaiian be ordered to specifically perform the basic agreement, as amended by the December 16 letter (R. 61-62).

Hawaiian answered and essentially alleged that Hawaiian had terminated the basic agreement in the manner permitted by that agreement by its letter of April 17, 1967 (Ex. P-10); that its Washington attorney, A. Harry Becker, had no authority to extend the termination date of the basic agreement; that it was ready and anxious to complete a sale of the television station to another purchaser at a greater price; and, that the

basic agreement as amended by the December 16 letter was not subject to specific performance (R. 64-68). Hawaiian also counterclaimed essentially alleging that it was suffering operating losses of approximately $700 per day and that Freindly's action taken subsequent to Hawaiian's termination of April 17, 1967, was causing Hawaiian to suffer these losses (R. 68-70).

Upon Hawaiian's motion (R. 53-59) and agreement of the parties, the Court, pursuant to Rule 65(a)(2) of the Federal Rules of Civil Procedure, advanced the trial of the action on its merits and consolidated the same with the hearing on Friendly's application for a preliminary injunction (R. 71-72).

By stipulation, it was agreed that trial of the issues raised by the counterclaim would be postponed (Tr. 2-3).

Facts:

On or about January 7, 1966, Hawaiian entered into the basic agreement with United Broadcasting Company, Inc., to sell and assign said FCC license, together with all the fixed and tangible assets of Hawaiian used or useful in the operation of station KTRG-TV. The basic agreement was subsequently assigned by United to Friendly with the knowledge and consent of Hawaiian (Ex. P-2g).

The basic agreement was prepared for the signatures of the parties and was signed in Honolulu on behalf of Hawaiian by its president, David Watumull. After the basic agreement was signed by Mr. Watumull, it was returned to

A. Harry Becker, Hawaiian's counsel in Washington, D. C., upon the express condition that the closing date (the date upon which the sale and assignment would be consummated and control of the station turned over to Friendly) would be changed from 45 days to 5 days after FCC approval of the sale and assignment (Ex. D-1) (Tr. 267-268).

On or about January 11, 1966, Mr. Becker and Stanley B. Cohen, a partner of the Washington, D. C. law firm of Cohn & Marks, counsel for United Broadcasting Company, Inc., agreed upon the change in the closing date specified by Mr. Watumull, and their agreement was set forth in a letter dated January 11, 1966, from Mr. Cohen to Mr. Becker (Ex. P-2f). This letter was signed only by Mr. Cohen as the attorney of United Broadcasting Company, Inc. The last paragraph of the letter asserted the following, however: "You [Mr. Becker] have also advised me that the substance of the foregoing provisions has been conveyed to seller and that seller is agreeable thereto." Morever, the letter was affixed as an exhibit to the seller's portion of the Application for Consent to the Assignment of the License (Ex. P-2a) at the time that the Application was signed by Mr. Watumull as president of Hawaiian (Tr. 269).

The Application for consent to transfer the license was filed with the FCC on February 3, 1966 (Admission No. 7, Hawaiian's Answer, R-65).

Pursuant to the basic agreement (Ex. P-1, p. 4), an escrow account in the amount of $25,000 was required to be established with the attorneys of the parties as joint escrow

agents. The depository bank was in Washington, D. C. and instructions concerning the disbursement of the account were contained both in the basic agreement and the letter of January 11, 1966 (Ex. P-2f). Only the details of choosing the depository and establishing the account were left to the attorneys Mr. Becker and Mr. Cohen, since the other terms of the escrow were already established in the two documents mentioned above.

Shortly prior to June 7, 1966, at the request of Mr. Watumull, Mr. Becker commenced negotiations to have Friendly put an additional sum into an escrow account at the Bank of Hawaii, Honolulu, Hawaii (Tr. 203). Mr. Becker initiated conversations regarding the escrow account with Friendly's attorneys (Tr. 204) and by letter dated June 7, 1966, to Mr. Cohen (Ex. P-3) confirmed recent telephone conversations in which an agreement had been reached as to the establishment of the escrow account. By letter dated June 8, 1966 (Ex. P-4), Mr. Cohen wrote to Mr. Becker and transmitted Friendly's check for $185,000. That letter (Ex. P-4) was not filed with the FCC (Tr. 112-113).

By letter dated June 9, 1966, Mr. Becker wrote to the Bank of Hawaii requesting the establishment of the escrow account (Ex. P-12a). A copy of the letter was simultaneously submitted to Mr. Watumull (Tr. 315).

Some time after June 22, 1966, Mr. Paul Dobin replaced Mr. Cohen and other memebers of his law firm as the attorney in charge of Friendly's portion of the Application pending

before the FCC. Prior thereto Mr. Dobin had not been personally involved in the negotiation of the January 11, 1966 letter (Ex. P-2f) or the June correspondence (Ex. P-3 and Ex. P-4) (Tr. 106-108).

When the Application was filed with the FCC on February 3, 1966, the parties contemplated that the sale would be consummated within about 90 to 120 days (Tr. 270). Friendly and its counsel were well aware that Hawaiian was very anxious to consummate the sale, and they knew that such anxiety was prompted by the fact that Hawaiian was suffering substantial operating losses of approximately $700 per day (Tr. 23; 31; 59; 110-111; 308). Notwithstanding Hawaiian's desire for prompt action, it became apparent that Friendly was having difficulty in satisfying the FCC's requirements, and from as early as March, 1966, Friendly was filing additional information in an attempt to satisfy these requirements (Tr. 53; 144-145). The additional information did not, however, satisfy the FCC and on September 30, 1966, the FCC ordered that the Application be designated for hearing (Ex. P-13). This meant that the FCC was unable to make a finding that it was in the public interest to assign the license and, as required by FCC rules, a hearing had to be held before the Application could be denied (Tr. 54). It also meant that the processing of the Application would be substantially delayed.

The delays caused in processing the Application were Friendly's fault, and the matters raised by the order

designating the Application for hearing (Ex. P-13) were all directed to Friendly (Tr. 119; 147).

On October 28, 1966 there was a pre-hearing conference, at which time Mr. Dobin became convinced that a decision on the Application was not possible before February 3, 1967 (Tr. 67), the first anniversary of the filing date of the Application and the earliest date upon which either party could give notice of termination of the basic agreement. Accordingly, Mr. Dobin, being concerned that there was inadequate time under the basic agreement to receive an initial decision by the examiner, began discussions with Mr. Becker concerning an agreement to extend the time period during which Hawaiian would stay in the case (Tr. 68-70). Nothing specific was discussed until a meeting held sometime in the latter part of November, 1966 between Mr. Dobin, Mr. Becker and Mr. Eaton, the president of Friendly (Tr. 70-72; 214). Certain terms and proposals discussed at such meeting were shortly thereafter reduced to writing by Mr. Dobin in a document entitled "Supplement to Agreement" (Ex. D-2), which was signed by Mr. Eaton and sent to Mr. Becker (Tr. 76).

Under letter dated December 2, 1966 (Ex. D-3), the Supplement was sent by Mr. Becker to Mr. Watumull for execution by him as president of Hawaiian (Tr. 213). The essential terms of the Supplement were that the basic agreement, terminable by either party after February 3, 1967, would not be terminable until December 31, 1967, if a final decision by the FCC on the Application had not been made

before said date. In addition, if the FCC approved the assignment and the sale were consummated, Friendly would indemnify Hawaiian for all net out-of-pocket losses up to $35,000 in the operation of the television station from September 28, 1966, until the grant of the Application. The $35,000 was to be paid upon execution of the Supplement by way of loan secured by a chattel mortgage.

Mr. Watumull rejected the Supplement and informed Mr. Becker of the rejection in a telephone conversation on December 7, 1966 (Tr. 283-284. See also notes on Ex. D-3). Mr. Becker promptly conveyed Mr. Watumull's rejection to Mr. Dobin (Tr. 77-78; 216).

During the period December 7 to 12, 1966 there were three conversations between Mr. Becker and Mr. Watumull and several between Mr. Becker and Mr. Dobin. Much testimony was adduced at the trial relating to such conversations and, inasmuch as much of that testimony goes to the basic issues of this appeal, it will be referred to in more detail in the Argument in this brief. It is, however, undisputed that the hearings before the FCC examiner commenced December 8, 1966 and continued on December 9, 12, 13 and 14, 1966 and January 9 and 13, 1967 (Tr. 87).

On December 16, 1966, Mr. Dobin wrote Mr. Becker the letter (Ex. P-6), which purported to extend the basic agreement for an indefinite time. That letter is the heart of Friendly's case. Mr. Becker admitted that he

signed the letter as counsel for Hawaiian immediately upon its receipt by him and that he immediately returned it to Mr. Dobin's office (Tr. 233). Mr. Dobin filed the letter with the FCC as part of the Application (Ex. P-8; Tr. 109). Mr. Dobin did not send a copy of the letter to Hawaiian (Tr. 110) even though the basic agreement (Ex. P-1, page 20; R. 31) required that all notices be sent to Mr. Becker and Mr. Watumull. Nor did Mr. Becker inform Mr. Watumull of the existence of the letter or of there being a written agreement extending the time of termination of the basic agreement (Tr. 243-244). Mr. Watumull first learned of the December 16 letter when Mr. Dobin enclosed a copy of it with his letter of April 19, 1967 (Ex. D-9) written in response to Hawaiian's termination letter of April 17, 1967 (Ex. P-10; Tr. 296).

Mr. Dobin admitted that he never inquired of Mr. Becker as to whether he had authority to make the agreement set forth in the December 16 agreement and Mr. Becker never told him that he had such authority (Tr. 103-105). In Mr. Becker's words: "To put it completely, the authority was never discussed." (Tr. 237).

On February 9, 1967, Mr. Watumull wrote Mr. Becker asking whether Hawaiian had the right to cancel the agreement with Friendly on five days' notice (Ex. D-4). By letter dated February 13, 1967, Mr. Becker gave his opinion that Hawaiian could give such notice of termination (Ex. D-5; D-6). The opinion letter made no mention of any agreement which extended or purported to extend the termination date of the basic agreement.

Subsequent to the receipt of said opinion letter, Mr. Watumull had several conversations with Mr. Becker in which termination of the basic agreement was discussed and each time Mr. Becker advised Mr. Watumull not to terminate until a new buyer had been obtained (Tr. 290-291).

Discussions with other possible buyers for the television station were carried on during February, March and April, with the knowledge and assistance of Mr. Becker (Tr. 290-293).

On April 17, 1967, Mr. Watumull discussed with Mr. Becker the letter of termination (Ex. P-10) that was sent on the same day to Friendly. Mr. Becker approved the letter and recommended the inclusion of an additional paragraph (Tr. 293-294). Mr. Becker confirmed this, but adds that he also suggested the return of the $5,000 he had received from Friendly (Tr. 236-237). On December 12, 1966, Mr. Dobin had transmitted to Mr. Becker Friendly's check payable to Mr. Becker in the sum of $2,500 (Ex. D-7; Tr. 81). On December 29, 1966, Mr. Dobin transmitted to Mr. Becker a second similar check (Ex. D-7; Tr. 88). At that time Mr. Watumull did not know that Mr. Becker had received payment (Tr. 302), and bills sent to Hawaiian by Mr. Becker's firm during the period January 3, 1967, to May 1, 1967, (Exs. D-8a through 8f) did not disclose the receipt by Mr. Becker of the $5,000. There was no explanation given as to why Friendly made payment directly to Mr. Becker when, according to Mr. Dobin, payment was supposed to be reimbursement to Hawaiian (Tr. 115-116).

The suit by Friendly against Hawaiian was filed on May 3, 1967. On June 30, 1967, a Judgment was entered enjoining Hawaiian from terminating the basic agreement or in any manner whatsoever interfering with the Application and provided that the Judgment and Order would remain in full force and effect until the initial decision of the FCC examiner (R.127). The Judgment was in substance a preliminary injunction and by its terms required that further action would be taken. Notice of Appeal from that Judgment was filed (R. 130), but it was dismissed by agreement of the parties (R. 142).

The initial decision of the FCC examiner was rendered on July 27, 1967. It consented to the transfer of the license to Friendly (Tr. 403-404). The decision of the FCC to consent to the transfer of the license became final on September 15, 1967 (Tr. 406-407).

On September 15, 1967, and at the earliest opportunity after the FCC decision became final, Hawaiian's counsel filed in open court a copy of a registered air mail letter dated September 15, 1967, which Hawaiian had signed and mailed to Friendly and others, and which gave notice of termination of the basic agreement as amended by the December 16 letter (R.150; Tr. 408). Hawaiian asserted that it did not agree with the Court's decision that it was bound by the December 16 letter, but inasmuch as the Court had so ruled, Hawaiian gave notice of termination as permitted by the clear terms of the December 16 letter. Hawaiian also orally moved the Court

for an order vacating the injunction and dismissing the action (Tr. 408). The oral motion was renewed in writing (R. 144-151). The Court denied the motion (Tr. 448-449).

On September 19, 1967, Final Judgment was entered essentially ordering Hawaiian to specificially perform the basic agreement, as previously amended, including the amendment of the December 16 letter, and ordered Hawaiian to do all acts necessary and proper to facilitate and consummate the sale, subject to the condition that Friendly reimburse Hawaiian for certain operating losses (R. 152-156). This Appeal was taken from that Final Judgment on October 19, 1967 (R. 174).

SPECIFICATION OF ERRORS

The United States District Court for the District of Hawaii committed manifest errors when it made the following Findings of Fact and Conclusions of Law:

1. The Court erred in holding that, at the time Mr. Becker signed the letter of December 16, 1966 (Ex. P-6), he had express authority from Hawaiian to do so; that he had good reason to believe that he had authority to do so on behalf of Hawaiian; and that Hawaiian was agreeable to the kind of agreement he was signing (R. 120-121, Finding of Fact No. 39).

2. The Court erred in holding that the letter of December 16, 1966, was an amendment to the basic agreement (Ex. P-1) and was binding on Hawaiian (R. 121, Finding of Fact No. 40).

3. The Court erred in holding that Mr. Dobin had a right to believe that most of Mr. Becker's instructions came by telephone from Mr. Watumull and were, accordingly, acted upon by Mr. Becker, and that Mr. Dobin had a right to rely on what Mr. Becker told him based on his (Mr. Becker's) numerous telephone conferences with Mr. Watumull (R. 121, Finding of Fact No. 42).

4. The Court erred in holding that under the totality of all the circumstances, Mr. Dobin had the right to believe that Mr. Becker had the authority to sign the letter of December 16, 1966 and that said agreement bound Hawaiian (R. 121-122, Finding of Fact No. 43).

5. The Court erred in holding that Mr. Becker did thoroughly discuss with Mr. Watumull the agreement set forth in the letter of December 16, 1966; that he did tell Mr. Watumull that there was an agreement that bound Hawaiian to stay in the FCC proceedings until a decision; and that Mr. Becker believed, and had reason to believe, that Mr. Watumull understood that Hawaiian was bound to stay in the FCC proceedings until a decision and what was meant by staying in the proceedings until a decision (R. 122, Finding of Fact No. 45).

6. The Court erred in holding that Friendly did go forward with the prosecution of the Application and the FCC hearings in reliance on Hawaiian's agreement to extend the termination date of the basic agreement beyond February 3, 1967 (R. 123, Finding of Fact No. 49).

Specification of error as to Finding of Fact No. 46 was inadvertently omitted from its proper sequence.

5 (A) The Court erred in holding that Mr. Becker told Mr. Watumull that Hawaiian was bound to stay in the FCC proceedings until the Hearing Examiner's decision unless Hawaiian successfully repudiated Mr. Becker's authority to enter the December 16, 1966 agreement (R. 122, Finding of Fact No. 46).

5 (B) The Court erred in holding that because Mr. Watumull made no attempts to repudiate Mr. Becker's authority before April 17, 1967, he (Mr. Watumull) and Mr. Becker thus agreed not to do anything until a new prospective buyer could be found (R. 122, Finding of Fact No. 46).

7. The Court erred in holding that the FCC certificate, license or permit to operate station KTRG-TV is a unique chattel or asset and that the other assets or chattels or property which Hawaiian contracted to sell to Friendly were flavored or tainted by the FCC operating permit (R. 123-124, Finding of Fact No. 51).

8. The Court erred in holding that the FCC license or permit to operate station KTRG-TV held by Hawaiian was a unique chattel and a contract to sell or assign said license or permit was subject to specific performance (R. 124, Conclusion of Law No. 5).

9. The Court erred in holding that the Agreement of January 7, 1966, was amended by the letter dated December 16, 1966 (R. 124, Conclusion of Law No. 6).

10. The Court erred in holding that notwithstanding the provisions of 47 CFR, Sec. 1.513, it was immaterial that none of said amendments was signed by an officer or director of each of the corporate parties thereto, and it was sufficient to bind said parties legally that said amendments were signed by the respective parties' attorneys (R. 124, Conclusion of Law No. 7).

11. The Court erred in holding that all of said amendments were signed by the parties' attorneys with the authority of their respective clients (R. 125, Conclusion of Law No. 9).

12. The Court erred in holding that each of said amendments was and is binding upon Friendly and Hawaiian (R. 125, Conclusion of Law No. 10).

13. The Court erred in holding that A. Harry Becker had express authority to sign the December 16, 1966 amendment on behalf of Hawaiian (R. 125, Conclusion of Law No. 11).

14. The Court erred in holding that insofar as Friendly and its counsel, Mr. Dobin, are concerned, Mr. Becker had the apparent authority to sign the letter of December 16, 1966, on behalf of Hawaiian (R. 125, Conclusion of Law No. 12).

15. The Court erred in holding that Friendly would suffer irreparable injury if Hawaiian was not enjoined from withdrawing, terminating or in any manner whatsoever interfering with said Application until an initial decision by the FCC Hearing Examiner (R. 125, Conclusion of Law No. 13).

16. The Court erred in holding that Friendly would suffer irreparable injury if Defendant was not enjoined from selling, attempting to sell, or negotiating for sale, without recognition of Friendly's prior rights, any or all of the property Defendant had contracted to sell and assign to Friendly (R. 125, Conclusion of Law No. 14).

17. The Court erred in holding that if Mr. Becker did any wrong, or if he failed to communicate properly with Hawaiian and one of two parties must suffer because of his acts or omissions, then Hawaiian, the party that gave him the means in which to act or omit to act, must bear the consequences of his wrongful or improper acts or omissions (R. 126, Conclusion of Law No. 16).

18. The Court erred in holding that the basic agreement as amended (Exs. P-2f, P-4 and P-6) was subject to specific

performance, at least to the point of filing of the FCC Hearing Examiner's decision (R. 126, Conclusion of Law No. 17).

19. The Court erred in holding that Friendly had proved all the material allegations of its Complaint, as amended, and was entitled to the relief granted, at least up to the point of the filing the FCC examiner's decision (R. 126, Conclusion of Law No. 18).

20. The Court erred in failing to hold that the basic agreement was terminated by Hawaiian's letter of April 17, 1967 (Ex. P-10).

21. The Court erred in failing to hold that the December 16 letter was terminated by Hawaiian's letter of September 15, 1967, and in denying Hawaiian's Motion for Order Vacating Injunction and Dismissing Action (R. 144-151; Tr. 448-449).

22. The Court erred in dismissing Hawaiian's counterclaim (R. 156, Paragraph 3 of Final Judgment).

QUESTIONS PRESENTED

1. Was there sufficient evidence for the District Court to hold that A. Harry Becker, Washington attorney for Hawaiian, had express authority to extend the date of termination of the basic agreement?

2. Was there sufficient evidence for the District Court to hold that A. Harry Becker had apparent authority to extend the date of termination of the basic agreement?

3. Did the District Court, after having held that the December 16 letter was binding on the parties, have the power

to ignore the plain and unambiguous language of that letter and to order specific performance of the agreement after it had been terminated by Hawaiian at the time expressly permitted by the December 16 letter?

4. Did Friendly sustain its burden and prove that it was entitled to the relief of specific performance of the basic agreement, as amended?

SUMMARY OF ARGUMENT

Hawaiian's Washington attorney, A. Harry Becker, had neither express nor apparent authority to enter into or bind Hawaiian by the agreement set forth in the December 16 letter, which purported to extend indefinitely the termination date of the basic agreement.

In the alternative, if it is held that the December 16 letter is binding upon the parties as an amendment to the basic agreement, then the agreement was terminated according to the clear and unambiguous terms of the December 16 letter by Hawaiian's letter of September 15, 1967.

In either case, the Judgment should be reversed and an order entered that the basic agreement was terminated by Hawaiian on April 17, 1967, or in the alternative, on September 15, 1967, and Hawaiian should be permitted to prove its counterclaim.

Lastly, if neither termination was effective, Friendly nevertheless did not prove that it was entitled to the equitable relief of specific performance and it should have been relegated to its remedy of damages at law.

ARGUMENT

I. THE EVIDENCE FAILS TO SUPPORT THE HOLDING THAT A. HARRY BECKER, WASHINGTON, D.C. ATTORNEY FOR HAWAIIAN, HAD EXPRESS AUTHORITY TO ENTER INTO THE AGREEMENT EMBODIED IN THE DECEMBER 16, 1966 LETTER.

The contention throughout the proceedings below and in this appeal has been and is that the principal in this case, Hawaiian, through its president-manager, Mr. Watumull (Tr. 350), did not authorize its Washington, D. C. attorney Mr. Becker to enter into and to sign the agreement embodied in the December 16 letter. By express authority is meant the power of an agent to affect the legal relations of his principal by acts done in accordance with the principal's express manifestations of consent to him. Restatement, Agency 2d, "Authority", §7.

The sequence of events leading up to and surrounding the proposal and rejection of the Supplement to Agreement (Ex. D-2) is set forth above in the Statement of the Case (p. 7). The Supplement had been prepared for the signature of an authorized representative of Hawaiian, presumably Mr. Watumull (Tr. 132), in accordance to prescribed FCC form (Title 47, Code of Federal Regulations, §1.513; see Appendix A). Evidently, Mr. Dobin and Mr. Becker knew that such an amendment to the basic agree- had to be signed in compliance with FCC rules by an authorized representative of Hawaiian and, of course, Mr. Becker was not such an authorized person. The Supplement was, however, rejected, and Mr. Watumull conveyed his rejection to Mr. Becker by telephone on December 7, 1967 (Tr. 280-281; see also notes on Ex. D-3).

Sometime between December 7 and December 16 Mr. Becker nevertheless agreed with Mr. Dobin to extend the termination date of the basic agreement. On December 16 Mr. Becker signed (Tr. 233), as counsel for Hawaiian, the December 16 letter which extended the termination date on terms substantially different from those proposed in the rejected Supplement. This letter was not read to Mr. Watumull, or sent to Hawaiian for signature or approval before Mr. Becker signed it, nor was a copy forwarded to Hawaiian after its execution (Tr. 233-234). Between December 7 and December 16 Mr. Becker and Mr. Watumull had three telephone conversations, two on December 7 and one on December 12 (Tr. 284, 331). The question is, therefore, whether between the rejection of the Supplement on December 7 and Mr. Becker's signing of the letter on December 16, Mr. Watumull gave Mr. Becker express authority to enter into and to sign the agreement embodied in the December 16 letter.

Mr. Becker never unequivocally stated that he was given express authority to bind Hawaiian to the terms of the December 16 letter. Indeed, he even admitted that he did not tell Mr. Watumull about all of the terms found in the letter. Mr. Becker testified that he did not, between December 7 and December 12, the date on which he made his verbal agreement with Mr. Dobin, tell Mr. Watumull what was agreed to in the December 16 letter, i.e., that Friendly would be satisfied if Hawaiian would not terminate the basic agreement until an initial decison and that, if the decison was favorable, Hawaiian would stay through the final commission action,

but if the decision was unfavorable, then Hawaiian could terminate immediately (Tr. 225-226). Mr. Watumull's testimony on this point is not inconsistent with Mr. Becker's. Mr. Watumull also testified that Mr. Becker never informed him that Hawaiian would be bound not to terminate until a final decision if the initial decision were favorable (Tr. 282-286). The December 16 letter provided, however, that not only was Hawaiian to be bound until an initial decison, but also until a final decision if the initial one was favorable.

Mr. Becker testified that at some time between December 7 and 12 he informed Mr. Watumull by telephone that Friendly wanted Hawaiian to stay through the hearing and that Friendly would pay Hawaiian's costs in the hearing (Tr. 227). According to Mr. Becker, Mr. Watumull's reply was to the effect that if Friendly was willing to pay for the hearing to go ahead (Tr. 227). This was no more than Mr. Watumull had agreed to do even prior to December, for back in October and November, 1966, after telephone conversations with Mr. Becker, Mr. Watumull had acknowledged that under the requirements of the basic agreement (R. 27) he had no choice but to cooperate with Friendly's desire to have a hearing before the FCC and at that time Mr. Watumull was informed that Friendly would pay Mr. Becker's legal fee for the hearing (Tr. 277-278). Mr. Watumull understood the hearing to be the proceedings to be held in Washington in December, and at no time did Mr. Watumull believe Hawaiian was to be bound after February 3, 1967 (Tr. 333-334). On the other hand, Mr. Becker explained that by "stay through the hearing" he meant the taking of testimony, the filing of the

proposed findings and reply findings, and the initial decision of the examiner (Tr. 217). Mr. Becker clearly admitted, however, that he did not explain to Mr. Watumull what "stay through the hearing" meant in any of their conversations between December 7 and December 16 (Tr. 227).

Mr. Becker made a verbal agreement with Mr. Dobin on December 12, 1966 (Tr. 217, 232, 254), but only to the effect that Hawaiian would be bound up to an initial decision (Tr. 217), not through a final decision (Tr. 218). Mr. Dobin drafted the December 16 letter (Tr. 80), and though the letter contained terms which bound Hawaiian even beyond an initial decision, which terms Mr. Becker admitted he had not discussed with Mr. Watumull (Tr. 225-226), upon receipt of Mr. Dobin's letter Mr. Becker signed the letter as counsel for Hawaiian and sent it back immediately to Mr. Dobin (Tr. 233). In order for an attorney to bind his client and to sign a written agreement on behalf of his client, he must be given express authority from his client. This is especially true where an attorney is compromising or settling a claim but the same rule applies even if no litigation is involved. 7 Am. Jur. 2d, Attorneys at Law, §126, p. 127; Salter v. Carter, 257 Ala. 216, 58 So. 2d 454; Birmingham Electric Co. v. Cochran, 242 Ala. 673, 8 So. 2d 171; National Bread Co. v. Bird, 226 Ala. 40, 145 So. 462. Some of the cases even call for "special authority". Birmingham Electric Co. v. Cochran, supra; Starling, Executor v. West Erie Avenue Building and Loan Association, 333 Pa. 124, 3 A 2d 387; see also 30 A.L.R. 2d 944, Part IV, Sec. 9, "Special Authority to Compromise".

In Northwest Poultry and Dairy Products Co. v. A. C. Fry Co., 27 Wash. 2d 35, 176 P. 2d 324, the

following instructions, with regard to the sale of a building: "Go ahead, make the deal." The attorney signed on behalf of his clients a contract to sell the building but did not send copies of the contract to his clients who in the meantime accepted another offer for the building. The court held that the clients' instructions did not authorize the attorney to enter into and sign a binding contract on behalf of the clients, and the contract would not be specifically enforced in the absence of a showing of ratification. The same result was reached in Carstens v. McReary, 1 Wash. 359, 25 P. 471. Similarly in this case, even if Mr. Watumull did tell Mr. Becker to go ahead with the hearing, this did not authorize Mr. Becker to sign the December 16 letter with its broad terms. Mr. Becker could not even have reasonably believed that he was authorized to sign the December 16 letter. He himself admitted that he had no such express authority:

> "Q Did you ever ask Mr. Watumull or any other officer of Hawaiian Paradise Park Corporation for authority to sign the December 16 letter?
>
> "A [Mr. Becker] No."

The testimony of Mr. Dobin, a witness for Friendly, does not aid in establishing that Mr. Becker had express authority to bind Hawaiian to the agreement set forth in the December 16 letter. On the contrary, it corroborates a conclusion that no express authority could possibly have been given to Mr. Becker.

Mr. Dobin testified that Mr. Becker notified him of Mr. Watumull's rejection of the Supplement in a telephone

conversation (Tr. 77). During the same conversation, Mr. Dobin said that he suggested new terms of extension and that Mr. Becker agreed to the extension terms which were subsequently set forth in the December 16 letter (Tr. 78-80). The exact date of this conversation, however, could not be pinpointed by Mr. Dobin except that it was most likely sometime between December 5-8, (Tr. 81-82) but, in any case, before December 12 (Tr. 81). Mr. Dobin's testimony is inconsistent with that of Mr. Becker, who repeatedly testified that he reached a verbal agreement with Mr. Dobin on December 12, 1966. Mr. Dobin further testified that he had had no discussions with Mr. Becker pertaining to whether Mr. Becker had authority to make the agreement contained in the December 16 letter and to sign the same (Tr. 104-105) and Mr. Becker confirmed this (Tr. 237).

Accepting Mr. Dobin's testimony as fact leads to the conclusion that Mr. Becker made the extension agreement without express authority since it was made in the same conversation in which Mr. Becker conveyed Mr. Watumull's rejection of the Supplement. Since Mr. Becker himself testified that he never fully explained to Mr. Watumull the terms upon which Hawaiian would stay in the hearing (Tr. 225-226), Mr. Becker could not possibly have had express authority to convey Mr. Watumull's rejection of the sale and to accept immediately a new extension proposal which would bind Hawaiian until an initial decision and beyond.

If all of the uncontradicted evidence relating to the conversations between Mr. Becker and Mr. Watumull and Mr. Becker and Mr. Dobin during the period December 7 through December 16 are considered in the light most favorable to Friendly, a finding that Mr. Becker had express authority to enter into and sign the agreement embodied in the December 16 letter would be clearly erroneous. The evidence shows that Mr. Becker did not have express authority to sign the letter and did not have express authority to agree to the terms of the letter and to make it a binding agreement.

Further evidence from which it may be inferred that Mr. Becker did not have express authority is discussed below.

Mr. Watumull was not informed of the December 16 letter until Hawaiian attempted to terminate the basic agreement on April 17, 1967 (Ex. P-10; Tr. 294) and, along with his reply thereto, (Ex. D-9) Mr. Dobin transmitted to Mr. Watumull a copy of the December 16 letter. Nor did Mr. Watumull know that on December 12, 1966, even before the December 16 letter had been signed, a check was drawn by Friendly payable to Mr. Becker in the amount of $2,500 (Ex. D-7); and that Mr. Becker subsequently received another $2,500 by check dated December 29, 1966 (Ex. D-7). Hawaiian was thus never in a position to repudiate the December 16 letter since it had no knowledge of it: Mr. Becker never sent a copy of the December 16 letter to Mr. Watumull (Tr. 234); he never read it to Mr. Watumull on the telephone (Tr. 234), and he did not recall ever telling Mr. Watumull of its existence (Tr. 235,

253-254). Even when, by letter dated February 9, 1967 (Ex. D-4), Mr. Watumull wrote to Mr. Becker on behalf of the Board of Directors of Hawaiian to request a written opinion as to whether Hawaiian then had the right to cancel its contract with Friendly and, by opinion letter dated February 13, 1967 (Ex. D-5), Mr. Becker replied, no reference to the December 16 letter was made:

> "Mr. Watumull, your president, has asked that I give you my opinion as to whether or not Hawaiian Paradise Park Corporation has a right to give notice of cancellation of its contract with Friendly Broadcasting Company, under which it was proposed that Friendly Broadcasting Company acquire by assignment the license and assets of Television Station KTRG-TV.
>
> "In my opinion, since February 3 and at anytime prior to the day the Commission grants the application Hawaiian Paradise Park Corporation may give notice of termination of the agreement between it and Friendly Broadcasting Company pursuant to the provisions of Paragraph 11 of the agreement."

Mr. Becker also testified that he did not in the phone conversations prior to Mr. Watumull's February 9 request for opinion recall informing Mr. Watumull that he had signed a written agreement extending the termination date (Tr. 252, 253). Under examination by the Court, Mr. Becker failed to give satisfactory explanations as to why he failed to inform Mr. Watumull of the December 16 letter (Tr. 253).

Mr. Becker stated that he told Mr. Watumull that Hawaiian was bound to stay in until an initial decision of the examiner and if Hawaiian wanted to disavow Mr. Becker's agreement, Hawaiian could then terminate after February 3 (Tr. 253), but

Mr. Becker himself felt that the agreement was not beyond his authority (Tr. 259). Mr. Becker then proceeded to aid Hawaiian in finding a new buyer for the television station (Tr. 290-293).

On April 17, 1967, Mr. Watumull read and discussed on the telephone with Mr. Becker a draft of a termination letter that Mr. Watumull intended to send to Friendly. Mr. Becker suggested the addition of a paragraph concerning the release of escrow funds and gave the names of those to whom the letter should be sent (Tr. 294). The letter (Ex. P-10) was mailed on the same day (Tr. 294).

Soon thereafter, Mr. Watumull received a reply from Mr. Dobin, dated April 19, 1967 (Ex. D-9), with a copy of the December 16 letter (Tr. 294-295). Mr. Watumull phoned Mr. Becker and informed him that he (Mr. Watumull) had never seen the letter and had not known anything about it (Tr. 296). Mr. Becker responded by telling Mr. Watumull not to worry about the letter and that he would get the application withdrawn from the Commission and would go ahead and proceed with working on the contract with Hazel Bishop (Tr. 296-297). How could Mr. Becker have advised Hawaiian, helped it to seek new buyers, and aided Mr. Watumull in the drafting of a termination notice when he knew that a notice of termination by Hawaiian would surely lead to litigation (Tr. 258) and also knew that he had signed a written agreement about which his client was not informed and which he believed to be valid? In other words, Mr. Becker advised his client that it could terminate its contract if it was willing to run the substantial risk

of a lawsuit in which he would be maintaining a position diametrically opposed to his own client!

Upon a consideration of the evidence during the crucial period between December 7 and 16 and the events transpiring subsequent thereto, it was clearly erroneous for the Court to conclude that Mr. Becker had express authority to enter into and sign the agreement embodied in the December 16 letter.

II. THE EVIDENCE FAILS TO SUPPORT THE HOLDING THAT A. HARRY BECKER HAD APPARENT AUTHORITY TO ENTER INTO THE AGREEMENT EMBODIED IN THE DECEMBER 16 LETTER.

Apparent authority arises only from the principal's manifestations to third parties and exists only if it is reasonable for the third person to believe that the agent has authority. Restatement, Agency 2d, §27

A good statement of the general rule of law is found in Quint v. O'Connell, 89 Conn. 353, 94 A. 288, 290:

> "Apparent and ostensible authority is such authority as a principal intentionally or by want of ordinary care causes or allows a third person to believe that the agent possesses. This authority to act as agent may be conferred if the principal affirmatively or intentionally, or by lack of ordinary care, causes or allows third persons to act on an apparent agency. It is essential to the application of the above general rule that two important facts be clearly established: (1) That the principal held the agent out to the public as possessing sufficient authority to embrace the particular act in question, or knowingly permitted him to act as having such authority; and (2) that the person dealing with the agent knew of the facts and acting in good faith had reason to believe, and did believe, that the agent possessed

> the necessary authority. The apparent power of an agent is to be determined by the acts of the principal, and not by the acts of the agent; a principal is responsible for the acts of an agent within his apparent authority only where the principal by his acts or conduct has clothed the agent with the appearance of authority, and not where the agent's own conduct and statements have created the apparent authority. The liability of the principal is determined in any particular case, however, not merely by what was the apparent authority of the agent but by what authority the third person, exercising reasonable care and prudence, was justified in believing that the principal had by his acts under the circumstances conferred upon his agent."

Measured by the criteria established by the foregoing general rule, the evidence does not support a holding that Mr. Becker had apparent authority to enter into the agreement to indefinitely extend the date of termination of the existing basic agreement.

There were no acts of the principal directly with Mr. Dobin. It is clearly established that Mr. Dobin never talked, corresponded or in any manner dealt with Mr. Watumull or any other officer, director or employee of Hawaiian, and that his dealings were exclusively with Mr. Becker (Tr. 102-103).

Mr. Dobin, under the guise of testimony, stated the indicia of apparent authority upon which he claimed to have relied. Those were: (1) Mr. Becker was and had been counsel for Hawaiian for many years in matters before the FCC and Mr. Becker acted as counsel in connection with the filing of Hawaiian's part of the Application with the FCC; (2) Mr. Becker had been designated as escrow agent by Hawaiian on two occasions; (3) Mr. Becker was listed as a person to be notified

in connection with official communications under the agreement; (4) Mr. Becker was dealing with something which was considered an incident of the FCC hearing; (5) Mr. Becker had, so far as Mr. Dobin knew, been authorized on two occasions on behalf of Hawaiian to modify the basic agreement; and (6) Mr. Becker told him that Mr. Becker had been communicating with Mr. Watumull about the subject matter of the agreement (Tr. 92-94). For those reasons, Mr. Dobin testified he believed that Mr. Becker had authority to make on behalf of Hawaiian the extension agreement set forth in the December 16 letter.

It is helpful to separately analyze the record as it relates to each of the claimed indicia of apparent authority.

(1) Mr. Becker was and had been counsel for Hawaiian for many years in matters before the FCC and Mr. Becker acted as counsel in connection with the filing of Hawaiian's part of the Application with the FCC.

Mere employment of an attorney confers no apparent authority upon him to settle or compromise an action or to bind his client by entering into a contract or modifying an existing contract. Particularly, the attorney-client relationship does not confer upon the attorney the authority to enter into any agreement which would surrender a substantial right of his client or impose new burdens upon the client. Nellis v. Massey, 108 Cal. App. 2d 724, 239 P. 2d 509; 7 C.J.S., Attorney and Client, §105, P. 931; Starling, Executor v. West Erie Avenue Building, 333 Pa. 124, 3A 2d 387; McKeague v.

Freitas, 40 Haw. 108; Kallen v. Pollock, 412 Pa. 281, 194 A. 2d 227; 30 A.L.R. 2d 944 (Supplementing 66 A.L.R. 108).

(2) Mr. Becker had been designated as escrow agent by Hawaiian on two occasions.

The duties of Mr. Becker as escrow agent were very specific and were expressly detailed in the escrow instructions established by the January 11, 1966 letter (Ex. P-2f) and June 7 and 8, 1966 letters (Ex. P-3 and P-4). As such escrow agent he clearly would have no authority to go beyond the escrow instructions. This Court can take notice of the fact that attorneys are many times named as escrow agents in matters relating to their client's affairs. It is neither reasonable nor prudent to believe that the appointment as an escrow agent confers upon such agent the apparent authority to enter into a substantial and material modification of a client's existing contract. Philadelphia v. Schofield, 375 Pa. 554, 101 A. 2d 625.

(3) Mr. Becker was listed as a person to be notified in connection with official communications under the agreement.

Such a designation is too insignificant to establish apparent authority in this case. It is significant to note in this connection that Mr. Becker was only one of two persons who were to be notified. The other person was Mr. Watumull (Ex. P-1, page 20; R. 31). Mr. Dobin apparently ignored that provision of the basic agreement when he failed to send a copy of the December 16 letter to Mr. Watumull.

(4) Mr. Becker was dealing with something which was considered an incident of the FCC hearing.

This alleged indicia of apparent authority is essentially similar to number (1) above and as asserted there, it does not constitute an act of the principal which would give rise to a reasonable belief that apparent authority existed to materially modify an existing contract. On the contrary, this aspect of the authority question raises a more fundamental and far-reaching issue which decisively militates against any finding of apparent authority.

Both Mr. Becker and Mr. Dobin are attorneys who specialize and have specialized for many years in FCC matters. As such, those gentlemen knew or should have known the rules and regulations of the FCC, including the rule which is set forth in 47 Code of Federal Regulations §1.513 (See Appendix A). Section 1.513 requires that: "applications, amendments thereto and related statements of fact required by the Commission shall be personally signed by the applicant,---; by an officer if the applicant is a corporation;---". Subsection b of Section 1.513 expressly requires that: "Applications, amendments thereto and related statements of fact required by the Commission may be signed by the applicant's attorney in cases of the applicant's physical disability or of his absence from the United States."

The testimony establishes that the December 16 letter was filed with the FCC as an amendment to the application (Tr. 109). Accordingly, both Mr. Dobin and Mr. Becker knew

or should have known that Section 1.513 applied and that the December 16 letter, not being signed by the principals, was or at least might have been invalid. Even if such rule would not *ipso facto* render the December 16 letter invalid, it is sufficient that it establishes that Mr. Dobin was not acting reasonably and prudently when he relied upon the signature of Mr. Becker on the December 16 letter because he knew or should have known that the FCC required a higher order of signature.

Mr. Dobin certainly relied on those FCC rules when he asserted that it was sufficient to serve a copy of the December 16 letter only upon Mr. Becker and he cited rule 1.47 (47 C.F.R. §1.47) in support of his position (Tr. 98-99). It can be inferred that the FCC rules were in mind when Mr. Dobin prepared the Supplement (Ex. D-2) for the signatures of the principals.

(5) Mr. Becker had, so far as Mr. Dobin knew, been authorized on two occasions on behalf of Hawaiian to modify the basic agreement.

Mr. Dobin's knowledge of the prior modifications, that is the letters of January 11, 1966 (Ex. P-2 f) and June 7 and 8, 1966 (Exs. P-3 and P-4) was second hand (Tr. 47). He admits that he was not involved in the case until after those agreements were reached and executed (Tr. 50-51); that he did not previously discuss those agreements with Mr. Becker (Tr. 107); that his knowledge of the circumstances surrounding the execution of those agreements came from the face of the agreements themselves (Tr. 108).

Besides, the circumstances surrounding those modifications of the basic agreement were substantially different from those attendant upon the negotiation and execution of the December 16 letter. First, both of those modifications were initiated by Mr. Watumull and negotiated by Mr. Becker with Mr. Watumull's express request and knowledge. Second, both of the modifications essentially ran in favor of and were for the benefit of Hawaiian.

The January 11 letter (Ex. P-2f) is completely distinguishable. Mr. Watumull specifically executed the basic agreement upon the condition that the closing date be changed (Ex. D-1). The face of the January 11 letter shows the express authority of Mr. Watumull. In any event, the January 11 letter was affixed as an exhibit to the Application at the time the Application was sent to and was signed by Mr. Watumull (Tr. 269). This latter fact also negates Friendly's contention that C.F.R. 1.513 was not honored by the parties on previous occasions.

The increase in the escrow amount established in June of 1966 was also done at the direction and with the knowledge of Mr. Watumull (Tr. 312-313). Other than the amount and bank, the terms of the agreement were merely those which had already been established by the January 11 agreement. The letter from Mr. Becker to Edwin A. Schneider, president of the Bank of Hawaii (Ex. P-12a) shows that when the account was established at the Bank of Hawaii a copy of the letter was sent to Mr. Watumull. It is thus apparent that Mr. Becker's duties

in connection with each of the escrow letters were ministerial and incidental and in any event were expressly authorized and approved. Two expressly authorized acts done by an agent are insufficient to justify an inference of apparent authority to subject the principal to liability by subsequent acts not expressly authorized. Smith Premier Typewriter Co. v. National Hartel Light Co., 72 Misc. 405, 130 N.Y.S. 136.

The second important point of difference is that in the cases of the January 11 and June modifications, the benefits ran in favor of Hawaiian. On the other hand the December 16 letter was a material modification of a basic contract which would have substantially modified and waived Hawaiian's basic rights.

(6) Mr. Becker told Mr. Dobin that he had been communicating with Mr. Watumull about the subject matter of the agreement.

There is no question but that Mr. Becker was communicating with Mr. Watumull about the subject matter of the agreement. However, considering the evidence it is unreasonable to conclude that Mr. Dobin could prudently have relied upon the fact that he knew Mr. Becker was communicating with Mr. Watumull.

In the latter part of November, Mr. Becker, Mr. Dobin and Mr. Eaton met and presumably agreed upon a modification of the basic agreement. Mr. Becker told Mr. Dobin and Mr. Eaton that he would recommend it to his client (Tr. 73). Mr. Dobin reduced at least part of the oral agreement to writing (Ex. D-2). Although the agreement, that is, the "flip of the coin" (Tr. 75) whereunder Friendly would reimburse Hawaiian up to $7,500 for

for legal fees was also made at that meeting, that matter was not mentioned in the Supplement (Ex. D-2). Mr. Dobin procured the signature of Mr. Eaton, as president of Friendly, and transmitted the Supplement to Mr. Becker so that he would forward it to Mr.Watumull (Tr. 76). Mr. Becker transmitted the agreement to Mr. Watumull (Ex. D-3). Mr. Watumull promptly rejected the Supplement, and Mr. Becker communicated the rejection to Mr. Dobin (Tr. 76-77).

Mr. Dobin said, after the November meeting, "I thought I had an agreement." (Tr. 74). He, of course, was wrong. Mr. Watumull rejected it and Mr. Dobin knew it. These circumstances should have caused Mr. Dobin to know that it was not sufficient merely to believe that an agreement he entered into with Mr. Becker would be acceptable to Mr. Watumull. It is submitted that this incident alone was sufficient to have conclusively placed Mr. Dobin on notice that he could not safely rely upon Mr. Becker and he needed the agreement of Mr. Watumull. It should have been the "danger signal" and suggested to Mr. Dobin he had the duty to proceed with caution. <u>Standard Acc. Ins. Co. v. Simpson</u>, 64 F. 2d 583 (4th Cir. 1933). The agreement which is embodied in the December 16 letter was made by Mr. Becker and Mr. Dobin in a single telephone conversation (Tr. 79-80; 129; 131). Certainly Mr. Dobin must have known or should have known that since he initiated the ideas as to what the terms of the new agreement would be, Mr. Becker had no way in which he could have previously discussed with or received from Mr. Watumull authorization

with respect to the new terms of that agreement. It simply is impossible to conclude or infer that Mr. Dobin could have reasonably believed that Mr. Becker had authority to enter into an agreement which was being suggested for the first time and which could not possibly have been communicated to Mr. Watumull.

Mr. Watumull had just rejected an agreement which would have extended the basic agreement to a fixed date and which would have compensated Hawaiian for at least $35,000 worth of the operating losses it suffered and would suffer since September 28, 1966. Having just rejected such an agreement, it is inconceivable to believe that Mr. Watumull would have agreed to an indefinite extension of the termination date of the basic agreement when the only consideration to be received was that Friendly would reimburse Hawaiian in a sum not to exceed $7,500 for its attorney's fees.

It is thus submitted that the evidence does not sufficiently support a holding that Mr. Becker had apparent authority to enter into the December 16 letter. After the rejection of the Supplement, there were certainly no acts of the principal upon which Mr. Dobin could rely as a basis for his believing that Mr. Becker had authority to enter into and sign an agreement materially modifying the basic agreement. As has been previously cited, it is necessary to establish apparent authority by the acts of the principal and not the acts of the agent.

It has been previously shown that Mr. Becker did not state to Mr. Dobin that he had authority and Mr. Dobin did not inquire whether Mr. Becker had authority. The risk of such failure is upon Friendly. National Bread Co. v. Bird, 226 Ala. 40, 145 So. 462:

> "All who deal with an attorney or other agent must ascertain the extent of his authority. If they do not inquire, they can claim no protection because they indulged suppositions or conjectures, reasonable or unreasonable, that the agent had the authority he was exercising."

See also, McKeague v. Freitas, supra; Starling, Executor v. West Erie Avenue Building, supra; Standard Acc. Ins. Co. v. Simpson, supra; Bank of Glade Spring v McEwen, 160 N.C. 414, 76 S.E. 222.

III. HAVING HELD THAT THE DECEMBER 16 LETTER WAS BINDING ON THE PARTIES, THE DISTRICT COURT HAD NO POWER TO IGNORE THE PLAIN AND UNAMBIGUOUS LANGUAGE OF THAT LETTER AND TO ORDER SPECIFIC PERFORMANCE OF THE AGREEMENT AFTER IT HAD BEEN TERMINATED BY HAWAIIAN AT THE TIME EXPRESSLY PERMITTED BY THE DECEMBER 16 LETTER.

A. IF THE DECEMBER 16 LETTER WAS BINDING ON THE PARTIES, HAWAIIAN HAD A RIGHT TO TERMINATE THE AGREEMENT ACCORDING TO THE CLEAR AND UNAMBIGUOUS LANGUAGE OF THE DECEMBER 16 LETTER.

On June 30, 1967, the District Court entered Findings of Fact and Conclusions of Law (R. 112-126). On that same date the Court also entered a Judgment (R. 127-129) wherein Hawaiian was enjoined from taking certain actions specified therein, including terminating the basic agreement. The Judgment by its terms contemplated further action by the Court and the Court expressly reserved jurisdiction in the cause (R. 129).

The parties stipulated (Tr. 403-404, 406-407) that subsequent to the entry of Judgment on June 30, 1967, the following events occurred with respect to the Application with the FCC: (1) On July 27, 1967, the FCC examiner's initial decision was released and it was in favor of the transfer of the license; and (2) the decision of the FCC consenting to the transfer of the license became final on September 15, 1967.

The Court concluded, as a matter of law, that the December 16 letter was binding upon both Friendly and Hawaiian (R. 125, Conclusion of Law No. 10). Hawaiian did not, and still does not, agree with that conclusion, but it had to recognize that it was bound by such holding on September 15, 1967. Accordingly, on September 15, 1967, which was the

earliest opportunity after the FCC decision became final, Hawaiian gave notice of immediate termination of the agreement with respect to the sale and purchase of KTRG-TV (R. 150; Tr. 408). On the same day Hawaiian also orally moved the Court for an order vacating the injunction and dismissing the action (Tr. 408). The oral motion was renewed in writing (R. 144-151). The Court denied the motion (Tr. 448-449) and entered its Final Judgment of specific performance on September 19, 1967 (R. 152-156).

Hawaiian based its right to terminate on the last sentence of the second paragraph of the December 16 letter, which paragraph in its entirety states as follows:

> "In consideration of our going forward promptly and diligently with the hearing and the prosecution of the application, Hawaiian Paradise has agreed not to terminate the pending sales agreement until such time as an initial decision shall be issued by the Examiner. If that decision should recommend a denial of the application, Hawaiian Paradise would be free to give Friendly notice of cancellation of the agreement. However, if the decision is favorable, you would not terminate the agreement until a final decision is rendered by the Commission."

The language of the last sentence of the above quoted paragraph is clear and unabmiguous and the Court had no power to ignore its plain meaning and subject the language to interpretation. The cases are legion in holding that a court may not resort to construction or interpretation where the agreement of the parties is expressed in clear and unambiguous language. 17A C.J.S. Contracts, §294(b); 17 Am. Jur. 2d, Contracts, §241;

Great Lakes Towing Co. v. Bethlehem Transp. Corporation, 65 F. 2d 543 (6th Cir. 1933); *Homelite v. Trywilk Realty Company*, 272 F. 2d 688 (4th Cir. 1959); *Ross v. Harding*, 64 Wash. 2d 231, 391 P. 2d 526; *Silen v. Silen*, 44 Wash. 2d 884, 271 P. 2d 674; *Atlas Sewing Center, Inc. v. Belk's Department Store*, Fla., 162 So. 2d 274; *Costiga Development Co. v. United Fuel Gas Co.*, 147 W.Va. 484, 128 S.E. 2d 626; *Southern Construction Company, Inc., v. United States*, 364 F. 2d 439 (Ct. Clms 1966); *Carter Oil Co. v. McCasland*, 190 F. 2d 887 (10th Cir. 1951), cert. den. 342 U.S. 870, 72 S.Ct. 113, 96 L. Ed. 654, reh. den. 342 U.S. 899, 72 S.Ct. 231, 96 L. Ed. 673; *K E C O Industries, Inc. v. United States*, 364 F. 2d 838 (Ct. Clms 1966), cert. den. 386 U.S. 958.

B. IF ARGUENDO, THE COURT COULD PROPERLY RESORT TO INTERPRETATION, IT REACHED THE WRONG MEANING OF THE LAST SENTENCE FOR THE FOLLOWING REASONS:

1. It Failed To Construe Any Doubtful Language Against The Draftsman.

The December 16, 1966, agreement was drafted by Mr. Dobin (Tr. 83-84), attorney for Friendly. The cases are also legion in holding that, if a contract must be interpreted because of doubtful language, the contract must be construed most strongly against the party who drew it. 17A C.J.S., *Contracts*, §324; 17 Am. Jur. 2d, *Contracts*, §276; *W. T. Rawleigh Co. v. Wilkes*, 197 Ark. 6, 121 S.W. 2d 886; *Couture v. Ocean Park Bank*, 205 Cal. 338, 270 P. 943; *Kinmonth v. Griffith*, 180 Kan. 389, 304 P. 2d 494; *Laue v. Grand Fraternity*, 132 Tenn. 235,

177 S.W. 941; Cedar Park Cemetery Ass'n. v. Calumet Park, 398 Ill. 324, 75 N.E. 2d 874; Green v. Royal Neighbors of America, 146 Kan. 571, 73 P. 2d 1.

2. Under The Guise Of Construction, It Improperly Wrote A New Contract For The Parties.

In effect, the Court rewrote the last sentence of the December 16 letter to read as follows: "However, if the decision is favorable, you would not terminate the agreement until a final decision is rendered by the Commission; provided that if the final decision is favorable you will not terminate at all and if the final decision is unfavorable, you can terminate but only upon five days' notice." (Oral Decision, (Tr. 423-431). The Court's attempted interpretation violates the fundamental principle that a court may not rewrite a contract under the guise of construction by inserting words which the parties have not used. 17 Am. Jur. 2d, Contracts, §242; Public Service Co. v. City and County of Denver, 153 Colo. 396, 387 P. 2d 33; Washington Constr. Co. v. Spinella, 8 N.J. 212, 84 A. 2d 617; McCall v. Carlson, 63 Nev. 390, 172 P. 2d 171. "It is elementary law, universally accepted, that the courts do not have the power, under the guise of interpretation, to rewrite contracts which the parties have deliberately made for themselves." Chaffee v. Chaffee, 19 Wash. 2d 607, 145 P. 2d 244. "In construing a letter, a court is not at liberty in order to fasten liability to add or take away words, thereby altering the sense, and either enlarging or cramping the assurance given in the

instrument." Liggett v. Levy, 235 Mo. 590, 136 S.W. 299. "Neither a court of law nor a court of equity can interpolate in a contract what the contract does not contain, either in words or by necessary implication." 17 Am. Jur. 2d, Contracts, §242, p. 629; Gavinzel v. Crump, 89 U.S. (22 Wall.) 308, 22 L. Ed. 783; Hudson Canal Co. v. Pennsylvania Coal Co., 75 U.S. (8 Wall.) 276, 19 L. Ed. 349.

The principles which prohibit a court from rewriting the parties' contract are particularly applicable to specific performance actions. Friendly prayed for specific performance of the basic agreement, as amended by the December 16 letter (R. 61-62). The Court cannot reform or rewrite the agreement and then specifically enforce it. O'Brien v. Fricke, 148 Neb. 369, 27 N.W. 2d 403; Brody v. W. & L. Enterprises, Inc. 117 N.Y.S. 2d 719, 4 Misc. 2d 907, aff'd 120 N.Y.S. 2d 239, 281 App. Div. 867; Waterman v. Banks, 144 U.S. 394, 12 S.Ct. 646, 36 L. Ed. 479.

3. It Failed To Consider The Material Evidence In Placing A Meaning Upon The Language.

The Court apparently placed some reliance on the April 17, 1967 letter (Ex. P-10) in construing the meaning of the language of the December 16 letter (Tr. 428-429). Such reliance was clearly misplaced because it was unequivocally established that when the April 17 letter was written by Mr. Watumull, he did not know of the existence of the December 16 letter.

If the Court could look to extrinsic evidence, it should have considered the April 19, 1967 letter of Mr. Dobin (Ex. D-9).

Mr. Dobin was, of course, the draftsman of the December 16 letter and it would seem that his interpretation of the language should have considerable weight. Mr. Dobin's letter of April 19, 1967 (Ex. D-9) confirms the meaning of the December 16 letter: "...this letter is to remind you of your obligation under the agreement of December 16, 1966 not to terminate the sales agreement until an initial decision shall have been issued by the Examiner and the Commission shall have had a final opportunity to pass upon the application for assignment of license."

Mr. Dobin's construction is consistent with the testimony. At no time was there considered or mentioned an obligation to stay in the proceedings or extend a termination date beyond the FCC's final decision (Tr. 60; 64; 68; 79).

The Court failed to properly consider that the requirement of FCC consent was merely permissive. Certainly a buyer or seller is not obligated to consummate a transfer of license merely because the FCC approves such a transfer. The parties never agreed to such an obligation and the Court has no power to impose such an obligation upon them.

IV. FRIENDLY FAILED TO SUSTAIN ITS BURDEN OF PROOF ON THE QUESTION AS TO WHETHER IT WAS ENTITLED TO SPECIFIC PERFORMANCE.

The burden of proof as to whether specific performance could be granted was on Friendly. 81 C.J.S. Specific Performance, §140. In order to prevail, Friendly had to

prove the inadequacy of the ordinary remedy of law, i.e. damages. <u>Walbergh v. Moudy</u>, 164 Cal. App. 786, 231 P. 2d 234. The applicable presumption in Friendly's case was that, if a breach of the basic agreement, as amended, had occurred, Friendly could be adequately compensated in damages.

> "In case of contracts for the sale or transfer of personal property, on the other hand, the presumption is that a breach of the agreement can be adequately compensated for in damages. Therefore, the plaintiff must allege facts which take the case out of the ordinary rule that contracts for the sale of personalty are not specifically enforceable because of the adequacy of legal remedy. He must not only allege irreparable injury, but set up a state of circumstances which if true show that the injury would be irreparable."

49 Am. Jur., <u>Specific Performance</u>, §163, p. 186; see also <u>Southern Iron & Equipment Co. v. Vaughan</u>, 201 Ala. 356, 78 So. 212; <u>Rimes v. Rimes</u>, 152 Ga. 721, 111 S.E. 34.

The only showings going to the right of specific performance were that Honolulu, Hawaii, is allotted four commercial channels and one educational channel (Tr. 14). Moreover, Mr. Eaton, president of Friendly, was interested in purchasing only stations in financial trouble because this had become a challenge to him (Tr. 21). No showing was made, however, that there were no other television stations avaialble for sale which would have fulfilled Mr. Eaton's requirements. No proof was made as to the inadequacy of damages as a remedy.

CONCLUSION

There is not sufficient evidence to sustain the District Court's holding that Mr. Becker had either express or apparent authority. If Friendly relied upon Mr. Becker, it was a misplaced reliance and one which it created and which it assumed the risk of by its failure to inquire as to the authority of Mr. Becker to bind Hawaiian to the agreement embodied in the December 16 letter.

If the Court sustains the holding that the December 16 letter is binding upon the parties, the Judgment should be reversed on the grounds that the agreement was properly and timely terminated by Hawaiian's letter of September 15, 1967.

Dated: Honolulu, Hawaii; March 9, 1968.

Respectfully submitted,

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CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

John Jubinsky

JOHN JUBINSKY

APPENDIX A

Title 47, Code of Federal Regulations, §1.511 and §1.513

... of this chapter: *Provided*, That ... interference shall be caused to other ... maintaining a regular operating ... within the experimental pe... unless the licensees of such other ... have previously consented ...

... FM broadcast station NDEA's permit such stations to operate, with their ... power and on their licensed frequency, in the State Defense Network ... of the State in which the FM station is located, to provide an alerting capability, and to aid in the restoration of normal communications facilities during and after an emergency.

(d) Remote pickup broadcast station NDEA's permit such stations to operate in a prescribed manner, on their licensed frequency and with normal power, in the State and local remote pickup broadcast intercommunication networks for intercommunication, cue and control, and program purposes during or after an emergency.

(e) Other NDEA's which may be issued will be on such terms as may be designated therein.

(f) All NDEA's are issued for periods of time covered by the station license of the station concerned, subject, however, to being changed or canceled at an earlier date in the discretion of the Commission without the necessity of a hearing.

(g) Unless canceled, National Defense Emergency renewal authorizations will be issued together with the station's renewal license.

General Filing Requirements

§ 1.511 Applications required.

(a) Except as provided in paragraph (b) of this section, construction permits as defined in section 3(dd) of the Communications Act of 1934, as amended; station licenses as defined in section 3(bb) of the Communications Act; modifications of construction permits or licenses; renewals of licenses; transfers; and assignments of construction permits or station licenses, or any rights thereunder, shall be granted only upon written and subscribed application. A separate application shall be filed for each instrument of authorization requested, except as may otherwise be provided in this part.

(b) In cases of (1) emergency found by the Commission involving danger to life or property or due to damage to equipment, or (2) during a national emergency proclaimed by the President or declared by the Congress and during the continuance of any war in which the United States is engaged, and when such action is necessary for the national defense or security or otherwise in furtherance of the war effort, the Commission may grant construction permits and station licenses, or modifications or renewals thereof, without the filing of a formal application; but no authorization so granted shall continue in effect beyond the period of the emergency or war requiring it.

(c) Each individual request submitted under the provisions of paragraph (b) of this section shall contain, as a minimum requirement, the following information:

(1) Name and address of applicant.

(2) Location of proposed installation or operation.

(3) Official call letters of any valid station authorization already held by applicant and the station location.

(4) Type of service desired (not required for renewal, nor for modification unless class of station is to be modified).

(5) Frequency assignment, authorized transmitter power(s), and authorized class(es) of emission desired (not required for renewal; required for modification only to the extent such information may be involved).

(6) Equipment to be used, specifying the manufacturer and type or model number (not required for renewal; required for modification only to the extent such information may be involved).

(7) Statements to the extent necessary for the Commission to determine whether or not the granting of the desired authorization will be in accordance with the citizenship eligibility requirements of section 310 of the Communications Act.

(8) Statement of facts which, in the opinion of the applicant, constitute an emergency to be found by the Commission for the purpose of this section, including the estimated duration of the emergency; or which, if during an emergency or war declared by the President or Congress, necessitate such action, without formal application, for the national defense or security or in furtherance of the war effort.

(Sec. 308, 48 Stat. 1084, as amended; 47 U.S.C. 308)

§ 1.512 Where to file; number of copies.

All applications for authorizations required by § 1.511 shall be filed at the Commission's main office in Washington, D.C. The number of copies required for each application is set forth in the FCC Form which is to be used in filing such application.

[29 F.R. 12371, Aug. 28, 1964]

§ 1.513 Who may sign applications.

(a) Except as provided in § 1.511(b) or in paragraph (b) of this section, applications, amendments thereto, and related statements of fact required by the Commission shall be personally signed by the applicant, if the applicant is an individual; by one of the partners, if the applicant is a partnership; by an officer, if the applicant is a corporation; or by a member who is an officer, if the applicant is an unincorporated association. Applications, amendments, and related statements of fact filed on behalf of eligible government entities, such as states and territories of the United States and political subdivisions thereof, the District of Columbia, and units of local government, including incorporated municipalities, shall be signed by such duly elected or appointed officials as may be competent to do so under the laws of the applicable jurisdiction.

(b) Applications, amendments thereto, and related statements of fact required by the Commission may be signed by the applicant's attorney in case of the applicant's physical disability or of his absence from the United States. The attorney shall in that event separately set forth the reason why the application is not signed by the applicant. In addition, if any matter is stated on the basis of the attorney's belief only (rather than his knowledge), he shall separately set forth his reasons for believing that such statements are true.

(c) Only the original of applications, amendments, or related statements of fact need be signed; copies may be conformed.

(d) Applications, amendments, and related statements of fact need not be submitted under oath. Willful false statements made therein, however, are punishable by fine and imprisonment, U.S. Code, Title 18, section 1001, and by appropriate administrative sanctions, including revocation of station license pursuant to section 312(a)(1) of the Communications Act of 1934, as amended.

(Sec. 308, 48 Stat. 1084, as amended; 47 U.S.C. 308)

§ 1.514 Content of applications.

(a) Each application shall include all information called for by the particular form on which the application is required to be filed, unless the information called for is inapplicable, in which case this fact shall be indicated.

(b) The Commission may require an applicant to submit such documents and written statements of fact as in its judgment may be necessary. The Commission may also, upon its own motion or upon motion of any party to a proceeding, order the applicant to amend his application so as to make the same more definite and certain.

(Sec. 308, 48 Stat. 1084, as amended; 47 U.S.C. 308)

§ 1.516 Specification of facilities.

(a) An application for facilities in the standard, FM, or television broadcast services shall be limited to one frequency, or channel assignment, and no application will be accepted for filing if it requests alternate frequency or channel assignments.

(b) An application for facilities in the experimental and auxiliary broadcast services may request the assignment of more than one frequency if consistent with applicable rules in Part 74 of this chapter. Such applications must specify the frequency or frequencies requested and may not request alternate frequencies.

(c) An application for construction permit for a new broadcast station, the facilities for which are specified in an outstanding construction permit, will not be accepted for filing.

(d) An application for facilities in the international broadcast service may be filed without a request for specific frequency, as the Commission will assign frequencies from time to time in accordance with §§ 73.702 and 73.711 of this chapter.

(Sec. 308, 48 Stat. 1084; as amended; 47 U.S.C. 308)

§ 1.518 Inconsistent or conflicting applications.

While an application is pending and undecided, no subsequent inconsistent or conflicting application may be filed by the same applicant, his successor or as-

APPENDIX B

TABLE OF EXHIBIT REFERENCES

Plaintiff's Exhibit	Identified	Offered	Received
P-1	Pre-Trial Conference (May 31, 1967)		
P-2a	"	"	"
P-2b	"	"	"
P-2c	"	"	"
P-2d	"	"	"
P-2e	"	"	"
P-2f	"	"	"
P-2g	"	"	"
P-3	"	"	"
P-4	"	"	"
P-5	"	"	"
P-6	"	"	"
P-7	"	"	"
P-8	"	"	"
P-9	"	"	"
P-10	"	"	"
P-11a	"	"	"
P-11b	"	"	"
P-11c	"	"	"
P-11d	"	"	"
P-11e	"	"	"
P-11f	"	"	"
P-12	Tr. 228	Tr. 229	Tr. 230
P-12a	Pre-Trial Conference (May 31, 1967)		
P-13	Tr. 84	Tr. 84	Tr. 85

Defendant's Exhibit	Identified	Offered	Received
D-1	Pre-Trial Conference (May 31, 1967)		
D-2	"	"	"
D-3	"	"	"
D-4	"	"	"
D-5	May 31, 1967	Tr. 261	Tr. 261
D-6	May 31, 1967	Tr. 261	Tr. 261
D-7	Pre-Trial Conference (May 31, 1967)		
D-8a	"	"	"
D-8b	"	"	"
D-8c	"	"	"
D-8d	"	"	"
D-8e	"	"	"
D-8f	"	"	"
D-9	"	"	"

No. 22394

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

HAWAIIAN PARADISE PARK CORPORATION,
a Hawaii corporation,

Appellant,

vs.

FRIENDLY BROADCASTING CO., INC.,
an Ohio corporation,

Appellee.

On Appeal from the United States District Court
for the District of Hawaii

APPELLANT'S REPLY BRIEF

STEPHENSON, ASHFORD & WRISTON
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Honolulu, Hawaii

Of Counsel

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Attorneys for Appellant
HAWAIIAN PARADISE PARK
CORPORATION

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TABLE OF AUTHORITIES CITED

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IN THE UNITED STATES COURT OF APPEALS

NINTH CIRCUIT

HAWAIIAN PARADISE PARK CORPORATION, a Hawaii corporation,	)
Appellant,	)
vs.	)
FRIENDLY BROADCASTING CO., INC., an Ohio corporation,	)
Appellee.	)

APPELLANT'S REPLY BRIEF

STATEMENT IN REPLY TO FRIENDLY'S REFERENCES TO EVIDENCE

In Appellee's Answering Brief, Friendly has referred without discussion to evidence which it claims supports the findings of fact which Hawaiian has designated as Specifications of Error Nos. (1), (4) and (7). The evidence referred to by Friendly does not support said findings of fact for the reasons already discussed in Appellant's Opening Brief.

In reply to the evidence referred to by Friendly in support of Specification of Error No. 1, Hawaiian incorporates herein by reference the Statement of the Case found in Appellant's Opening Brief, Pages 1 through 12, inclusive, and the additional statements of fact and discussion at Pages 18 through 27, inclusive, therein.

In reply to the references to evidence by Friendly as to Specification of Error No. 4 on Pages 3 and 4 of its

Answering Brief, Hawaiian incorporates herein by reference, in addition to its Statement of the Case referred to above, the additional statements of fact and discussion found on Pages 27 through 37, inclusive, of Appellant's Opening Brief.

Hawaiian has complied with Paragraphs 2(d) and (e) of Rule 18 of this Court in including in its Opening Brief a Specification of Errors, which states as particularly as may be wherein certain findings of fact and conclusions of law are alleged to be erroneous and which is followed by a Summary of Argument and a concise Argument of the case, which points out grounds for each specification of error. While each specification of error is not separately and chronologically discussed, each is specifically dealt with at some point in the Opening Brief. In any case, Hawaiian, if it has failed to discuss any of the specifications of error in its Opening Brief or this Reply Brief, nevertheless expressly reserves its right to orally argue the same. Western Nat. Ins. Co. v. Le Clare, 163 F.2d 337 (9th Cir., 1947).

ARGUMENT

I. HAWAIIAN'S WASHINGTON ATTORNEY, A. HARRY BECKER, HAD NEITHER EXPRESS, IMPLIED NOR APPARENT AUTHORITY TO ENTER INTO OR BIND HAWAIIAN BY THE AGREEMENT SET FORTH IN THE DECEMBER 16 LETTER, WHICH PURPORTED TO EXTEND INDEFINITELY THE TERMINATION DATE OF THE BASIC AGREEMENT.

A. EXPRESS AUTHORITY.

Express authority, whether oral or written, must be, according to Friendly's quotes, "distinct", "plain", "direct"

and "explicit". One searches in vain, however, for such authority in the transcript or the record.

Indeed, the transcript reveals that Mr. Becker himself admitted that he had no express authority to enter into the terms found in the December 16 letter:

> "Q Did you ever ask Mr. Watumull or any other officer of Hawaiian Paradise Park Corporation for authority to sign the December 16 letter?"
>
> "A [Mr. Becker] No." (Tr. 237)

Before the December 16 letter was signed by Mr. Becker, the letter was neither read to Mr. Watumull nor sent to Hawaiian for signature or approval (Tr. 233-234). After the letter was signed, Mr. Becker did not inform Mr. Watumull of its existence (Tr. 243-44), did not read it to the latter, and did not even forward a copy to Hawaiian (Tr. 233-234).

Nowhere in the transcript does Mr. Becker state that he was given express authority to sign and to bind Hawaiian to the terms of the December 16 letter. Mr. Becker did testify that he and Mr. Dobin had reached a verbal agreement prior to December 16, 1966, to the effect that Hawaiian would be bound up to an initial decision, not through a final decision (Tr. 217-218). Admitting that he had not discussed its terms with Mr. Watumull (Tr. 225-226), Mr. Becker, nevertheless, signed the December 16 letter which bound Hawaiian beyond an initial decision. Express authority cannot be based upon such facts, yet on Page 7 of its Answering Brief, Friendly points to evidence from which

it claims the judge could reasonably have inferred that Hawaiian had knowledge of the December 16 letter, even though as mentioned above, Mr. Watumull testified he had no knowledge of the December 16 letter until April 19, 1967 (Ex. D-9), after Hawaiian had written its termination letter (Ex. P-10).

The evidence referred to on Page 7 of the Answering Brief is irrelevant to the issue of Hawaiian's knowledge of the December 16 letter:

Paragraph 1 on Page 7. Nothing can be made of the presence of Hawaiian's attorney at the F.C.C. hearings, for Hawaiian's cooperation was necessary under the basic agreement. (Ex. P-1, Page 16; R. 27)

Paragraph 2. The fact that two of Hawaiian's employees testified before the hearing examiner cannot establish Hawaiian's knowledge of the December 16 letter, especially when one of the employees stated that he had testified and was back in Honolulu by December 13 (Tr. 365).

The actions of Hawaiian as stated in Paragraphs 3, 4, 5 and 6 were not inconsistent with a lack of knowledge of the December 16 letter, nor can they establish by inference any such knowledge on the part of Hawaiian.

Paragraph 7. As for the $5,000 attorney's fees paid to Mr. Becker, Mr. Watumull did not learn of the fact that such fees had been paid until May 15, 1967 (Tr. 302). Mr. Becker had, moreover, informed Mr. Watumull in October or November, 1966, that Friendly

would pay Mr. Becker's legal fees for the hearing. The hearings were not completed until early January, yet on December 12, 1966, before the December 16 letter had been signed, a check was drawn by Friendly payable to Mr. Becker in the amount of $2,500 (Ex. D-7). Another check dated December 29, 1966, also in the amount of $2,500, was subsequently given to Mr. Becker (Ex. D-7), before the hearings were completed.

B. IMPLIED AUTHORITY.

The facts of this case neither raise the issue of implied authority nor support a finding of the same. The signing of the December 16 letter cannot be said to constitute a merely "incidental" act in the absence of any oral express authority to enter into the agreement embodied in the December 16 letter.

Contrary to Friendly's statements in Paragraph (.) on Page 9 of its Answering Brief, the past actions of Hawaiian do not support a finding of implied authority. Each of the past actions referred to had either been expressly authorized by Hawaiian or expressly ratified. Furthermore, the authority to negotiate cannot be claimed to include implied authority to enter into a detrimental written agreement binding upon a principal with no knowledge of the agreement (see discussion and authorities in Appellant's Opening Brief, pages 21-27, 29-30).

C. APPARENT AUTHORITY.

Friendly supplies extensive quotations on apparent authority and cites and discusses several cases dealing with situations in which apparent authority was in issue. All of the cited cases are inapposite. The cases deal for the most part with ordinary sales cases and are not applicable to the instant case. None of the cited cases involves the apparent authority of an attorney.

No indicia of apparent authority are singled out in discussion by Friendly except that Hawaiian was required by distance, F.C.C. rules, and its corporate status to retain counsel. Hawaiian, on the other hand, has cited in its Opening Brief (pp. 28-29) several indicia of apparent authority upon which Mr. Dobin claims to have relied, none of which, taken separately or together can establish the requisite apparent authority. In that discussion Hawaiian cites numerous authorities which confirm that the mere employment and retention of an attorney, such as Mr. Becker, does not confer apparent authority on the attorney to enter into agreements such as that found in December 16 letter (Opening Brief, pp. 29-30).

II. SPECIFIC PERFORMANCE.

Friendly now states that, on the basis of Mr. Courtney's $250,000 approximation of the value of the fixed assets which Hawaiian agreed to sell, $300,000 should be the value

to be applied to the operating license (Answering Brief, p. 16). No testimony supports such a valuation for the operating license and Mr. Courtney did not give the operating license any such value (Tr. 11-14). Friendly has not shown, moreover, whether Mr. Courtney would even have been qualified to give an evaluation of the operating license. Any statements as to the value of the operating license are, therefore, sheer conjecture and of no probative value.

The fact that Honolulu, Hawaii, is allotted only four commercial channels and one educational channel does not by itself establish the uniqueness of the chattel upon which the right of specific performance must be founded. No other testimony as to what made the particular channel involved unique was adduced at trial.

III. HAWAIIAN HAS NOT WAIVED ITS RIGHT TO BE HEARD ON APPEAL.

Hawaiian hereby resubmits its Answer to Appellee's Motion to Dismiss Appeal, which motion was filed herein on January 8, 1968, and incorporates herein by reference said answer, served herein on Appellee's attorneys on January 12, 1968, and filed herein subsequent thereto, together with its supporting statement of facts, memorandum of points and authorities and exhibits.

CONCLUSION

There is insufficient evidence in the record to sustain the District Court's holding that Mr. Becker had express,

implied or apparent authority to enter into or bind Hawaiian by the agreement set forth in the December 16 letter.

If this Court sustains the holding that the December 16 letter is binding upon Hawaiian, then the agreement should be found, nevertheless, to have been terminated according to its clear and unambiguous terms by Hawaiian's letter of September 15, 1967.

The Judgment herein be reversed and an order entered to the effect that the basic agreement was terminated on April 17, 1967, or in the alternative, on September 15, 1967, and that Hawaiian be permitted to prove its counterclaim in either case.

If this Court holds that neither termination was effective, the case should be reversed and remanded on the grounds that Friendly did not prove that it was entitled to specific performance and Friendly should be relegated to remedy of its damages at law, if any.

Dated: Honolulu, Hawaii; September 3, 1969.

Respectfully submitted,

John Jubinsky

JOHN JUBINSKY

Galen C. K. Leong

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Of Counsel

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

John Jubinsky

JOHN JUBINSKY

No. 22,395

IN THE

United States Court of Appeals
For the Ninth Circuit

SHAFFER C. TIM, *Appellant,* vs. AMERICAN PRESIDENT LINES, LTD., a corporation, *Appellee.*	

Appeal from an Admiralty Decree of the
United States District Court for the
Northern District of California

Honorable Lloyd H. Burke, District Judge

APPELLANT'S BRIEF

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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No. 22,395

IN THE

United States Court of Appeals

For the Ninth Circuit

SHAFFER C. TIM,
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vs.
AMERICAN PRESIDENT LINES, LTD.,
a corporation,
Appellee.

Appeal from an Admiralty Decree of the United States District Court for the Northern District of California

Honorable Lloyd H. Burke, District Judge

APPELLANT'S BRIEF

The following findings of fact and conclusions of law are set forth by the court in its Findings of Fact in the Clerk's Transcript on file herein.

I

FACTS

The plaintiff, Shaffer C. Tim, was employed by defendant as a seaman aboard the SS. PRESIDENT TYLER in the capacity as chief electrician and was

so employed on February 2, 1965 when he suffered an accident in the course and scope of his employment. (Findings of Fact No. 2.)

The defendant, American President Lines, Ltd., owned and operated the SS. PRESIDENT TYLER. On the date of the accident, February 2, 1965, cargo at the No. 4 hatch of the SS. PRESIDENT TYLER was being worked by employees of Matson Terminals, Inc. The loading and unloading of the cargo then aboard the SS. PRESIDENT TYLER was done pursuant to a contract between the United States Government and American President Lines and pursuant to a contract between the United States Government and Matson Terminals. These contracts were not regarded by the trial judge as having significance insofar as the judgment reached by that court was concerned. (Findings of Fact No. 3.)

The cargo was being worked by use of a mechanical apparatus known as a gantry crane. The gantry crane was operated from a cab mounted upon the crane about 30 feet above the weather deck and over the No. 4 hatch. The "operating unit" relevant to this action consisted of the operator's cab, the controls to operate the crane inside the cab, a steel mesh platform to starboard and outside of the operator's cab, and a safety screen which, when in the "non-operating" position, lay over the top of the operator's cab and, when in the "operating position", extended over the platform outside the operator's cab. (Findings of Fact No. 6.)

In order to enter the operator's cab it was necessary to descend four steps, each step consisting of one horizontal steel bar, to reach the mesh platform. Once on the steel mesh platform one would turn left and enter through a door to the operator's cab, which was approximately 5 feet square. Inside the operator's cab were the controls of the gantry crane and a chair which faced forward away from the entry door to the operator's cab and from which the gantry crane operator would operate the gantry crane. (Findings of Fact No. 6.)

The plaintiff, Shaffer C. Tim, had worked on board the SS. PRESIDENT TYLER less than 7 days and had never worked on a vessel that had a gantry crane prior to signing aboard the SS. PRESIDENT TYLER. (Findings of Fact No. 7.)

The gantry crane operator's cab had a safety screen over the top of it which, if extended to its starboard-most position, engaged an electrical circuit which energized the gantry crane and allowed it to operate. When the safety screen was moved about 2 to 3 inches to port from its "operating position" the electrical circuit was de-energized and the gantry crane unit would not operate. (Findings of Fact No. 8.)

The safety screen in question had been installed by the defendant as a result of there having been an injury involving the operation of the gantry crane previous to that occurring to the plaintiff. This injury occurred before any safety screen was provided and led to the installation of the safety screen in

existence at the time of the injury occurring to the plaintiff. (Findings of Fact No. 9.)

The distance between the safety screen and the steel mesh platform below it when the safety screen was extended over the platform was less than 5 feet 6 inches. The plaintiff was 5 feet 6 inches tall. The safety screen was not large enough to prevent partial physical egress from the steel mesh platform and it was physically possible for the safety screen to have been larger. (Findings of Fact No. 16.)

At about 8:30 a.m. on February 2, 1965 a supervisory employee of Matson Terminals, Inc., the stevedoring company, complained to plaintiff that the gantry crane was not operating fast enough and requested plaintiff to remedy that situation. Pursuant to that request, plaintiff went to the operator's cab of the gantry crane (which was then occupied by Harry Johnson) and made adjustments which allowed the gantry crane to move athwartship at a faster speed. (Findings of Fact No. 12.)

After plaintiff made the necessary adjustments to allow the gantry crane to move faster, he stood behind Harry Johnson (the stevedore's employee assigned to operate the gantry crane). At the time the plaintiff was standing behind Harry Johnson he was inside the operating cab and was observing the gantry crane operation. Plaintiff then noticed that an electrical cable leading to another portion of the gantry crane had become disengaged from its reel and he told Harry Johnson, the gantry crane operator, that he

wanted to inspect the electrical cable. (Findings of Fact No. 13.)

In response to plaintiff's request Harry Johnson, the gantry crane operator, brought the gantry crane to a stop. (Findings of Fact No. 13.)

After waiting for the crane operator, Harry Johnson, to stop the crane, plaintiff then proceeded to the steel mesh platform outside the operator's cab. (Findings of Fact No. 14.)

At that time the safety screen above the steel mesh platform was at its starboardmost position, which allowed the gantry crane to operate. In order to inspect the electrical cable plaintiff, by placing his feet on the second rung of the ladder leading to the platform and placing his head outside the safety screen, was able to and did put his head into the space outside the screen, without placing the safety screen in a nonoperative position, and thus shutting off the power of the gantry crane. (Findings of Fact No. 14.)

The plaintiff relied on Harry Johnson, the operator of the gantry crane, not operating the crane while plaintiff was in this position and pursuant to plaintiff's requesting Harry Johnson to bring the gantry crane to a halt and the gantry crane thus being brought to a halt before plaintiff placed himself in this position. (Findings of Fact No. 14.)

While plaintiff had his head outside the safety screen the gantry crane operator started the gantry crane and plaintiff's head was caught and injured between the outboard portion of the safety screen and

a stationary overhead object which came into contact with plaintiff's head because of movement of the gantry crane. (Findings of Fact No. 14.)

II

ISSUES

A. DEFENDANT, AMERICAN PRESIDENT LINES, LTD., IS LIABLE FOR THE NEGLIGENT ACT OF THE STEVEDORE'S EMPLOYEE PERFORMED IN THE COURSE AND SCOPE OF HIS EMPLOYMENT ON BOARD THE DEFENDANT'S VESSEL.

The trial court, in its Findings of Fact and Conclusions of Law, stated the following:

> "1. Matson Terminals, Inc. was not the agent of American President Lines within the meaning of the common law agency concept or of 45 U.S.C., Section 51, as interpreted by the Supreme Court cases of *Sinkler v. Missouri Pacific Railroad Company,* 356 U.S. 326 (1958) and *Hopson v. Texaco,* 383 U.S. 262 (1966) and was therefore, not performing operational activities of the respondent at the time of the accident.
>
> "2. It was negligent of the gantry crane operator to operate the gantry crane when plaintiff was on the platform outside the operator's cab under the circumstances described.
>
> "3. At all material times the gantry crane was operated by Harry Johnson, an employee of Matson Terminals, Inc.
>
> "4. The loading and unloading of the cargo then aboard the SS. PRESIDENT TYLER was done pursuant to a contract between the United States Government and American President Lines

> and pursuant to a contract between the United States Government and Matson Terminals, Inc. These contracts were not regarded by the trial judge as having significance insofar as the judgment reached was concerned."

In addition to the above findings, the trial court made some pertinent statements relative to its positions and observations as to the law controlling in this matter:

> "The Court: I would have no difficulty with the case were it not for some implications in the *Hopson* case. However, there is a valid cause for distinction on the basis that the taxicab driver was the agent of the vessel performing a function which the vessel was legally obligated to perform, which would be the means by which you could distinguish those cases upon which Mr. Graham relies." (See R.T. dated March 29, 1967 at page 42, lines 21 through 25.)

> "The Court: I think you are right. I would have difficulty in reaching the decision that the Supreme Court reached in its ultimate decision on the case [*Hopson v. Texaco, Inc.,* 383 U.S. 262, 86 S. Ct. 765]. But as I have been reminded on other occasions, I am not in the Supreme Court." (See R.T. dated March 29, 1967, page 46, lines 4 through 8.)

> "The Court: Well, I think in order to find in favor of the libelant in this case, I would almost have to go the full route and say whatever happens to a seaman on board a vessel, regardless of what the conduct may be, the vessel is liable. I don't think the law has reached that point, although I may be very much in error." (See

R.T. dated March 29, 1967, page 48, lines 12 through 17.)

It is submitted that the court's comments obviously show the court's failure to recognize that the holding in *Hopson v. Texaco, Inc.,* 383 U.S. 262, 86 S. Ct. 765 (1966), does not stand for the proposition that a ship is liable for any injuries, regardless of the conduct giving rise to the injuries, that occurred to a seaman on board a vessel.

In the *Hopson* case, supra, the court held:

> "The Jones Act incorporates the standards of the Federal Employers Liability Act as amended which renders an employer liable for the injuries negligently inflicted on its employees by its 'officers, agents or employees'. We noted in *Sinkler v. Missouri Pacific Railroad Company,* 356 U.S. 326, 78 S. Ct. 758, 2 L. Ed. 2d 799, that the latter act was an avowed departure from the rules of the common law which, recognizing the cost of human injury and an inescapable expense of railroading, undertook to adjust that expense equitably between the worker and the carrier. In order to give an accommodating scope . . . to the word 'agents' we concluded that when (an) . . . employee's injury is caused in whole or in part by the fault of others performing under contract, operational activities of his employer, such others are agents of the employer within the meaning of Section 1 of FELA." (383 U.S. at pages 263-264.)

The court went on to state:

> "Getting these two ill seamen to the United States Counsel's office was therefore the duty of

respondent. And it was respondent—not the seamen—which selected, as it had done many times before, the taxi service. Respondent—the law says—should bear the responsibility for the negligence of the driver which it chose. This is so because as we said in *Sinkler,* justice demands that one who gives his labor to the furtherance of the enterprise should be assured that all combining their exertions with him in the common pursuit will conduct themselves in all respects with sufficient care that his safety while doing his part will not be in danger." (383 U.S. at page 264.)

This concept was more specifically referred to in the case of *Sinkler v. Missouri Pacific Railroad Company,* 356 U.S. 326, 78 S. Ct. 758, wherein the court stated:

> "It was the concept of Federal Employers Liability Act that the railroad was a unitary enterprise, and that its economic resources were obligated to bear the burden of all injuries befalling those engaged in the enterprise *arising out of the fault of any other member engaged in the common endeavor.*" (Emphasis added.) 356 U.S. at page 330.

The proposition set forth in the *Hopson* and *Sinkler* decisions, supra, limits the scope of liability of the vessel to injuries incurred as the result of negligence on the part of an individual "engaged in the common endeavor" or "operational activities" of the vessel.

The findings of the trial court below conclude that a longshoreman (the stevedore's employee) working

on board defendant's vessel in the scope and course of his employment of unloading cargo from the vessel is not engaged in the "common endeavor" or the "operational activities" of the vessel.

The trial court erred in failing to recognize that a longshoreman working on board defendant's vessel unloading defendant's cargo was clearly engaged in the ship's "operational activities" as set forth in the *Hopson* case, supra. The court erroneously concluded, as set forth above, that to hold that a longshoreman under such circumstances comes within the definition of "operational activity" would be to hold that whatever happened to a seaman, *regardless of what the conduct was,* would constitute liability. (Emphasis added.)

The instrumentality involved in causing injury to a seaman in *Hopson v. Texaco, Inc.,* supra, was that of an independent contractor (a taxi driver) whose services were secured for the purpose of transporting a disabled merchant seaman from his vessel to a local doctor. The taxicab driver was negligently involved in an automobile accident causing injury to the seaman.

In *Sinkler v. Missouri Pacific Railroad Company,* supra, the Supreme Court of the United States held that where defendant railroad's car, while under control of switching company's switching crews, was being handled to further the task of defendant railroad's enterprise, defendant railroad was liable for injury to its employee caused by fault of switching

company's employees, even if switching company was not under control of defendant railroad, in view of the fact that switching company, while engaged in such operations was an agent of defendant railroad within the meaning of the Federal Employers Liability Act.

Thus the Supreme Court recognized that the rule pertaining to "operational activity" turns on the question of whether the negligent party was engaged in furthering the "common endeavor" and did not turn on whether the defendant in fact had control of the negligent party. "This is so because as we said in *Sinkler,* justice demands that one who gives his labor to the furtherance of the enterprise should be assured that all combining their exertions with him in the common pursuit will conduct themselves in all respects with sufficient care that his safety while doing his part will not be in danger." (See: *Hopson v. Texaco, Inc.,* supra, 383 U.S. at page 263.) (See also: *Leek v. Baltimore and Ohio Railroad Company,* 200 F. Supp. 368; *Carney v. Pittsburgh and Lake Erie Railroad Company,* 316 F. 2d 277.)

The recognition by the Supreme Court that the shipowner has a non-delegable duty and cannot avoid that responsibility by arguments of independent contractor, lack of control over the negligent party, or that the equipment used by the longshoreman is not defective, was most recently reiterated in the case of *Mascuilli v. United States,* 387 U.S. 237, 1967 A.M.C. 1702.

The question in *Mascuilli,* supra, presented to the Supreme Court on certiorari was:

> "Does dangerous condition caused by stevedore's negligent handling of proper equipment render vessel unseaworthy and its owner liable for resulting injuries?"

In the *Mascuilli* case, supra, a longshoreman, Mascuilli, had been killed during a loading operation when one or more of his fellow longshoremen negligently caused both the starboard and port vangs on the loading boom to become taut simultaneously, thus causing one of the vangs to break. The parts thereof fell on Mascuilli, who had been engaged in a different aspect of the loading operation, and inflicted mortal wounds. The District Court sitting without a jury expressly found that the loading equipment was in a sound and safe condition. Finding of Fact No. 35 read as follows:

> "No. 35. In summary, the court finds that the vessel and all of its equipment was in a seaworthy condition at all times, and remained so throughout the entire loading operations. The accident was caused solely by the negligent operation of the stevedoring crew using seaworthy equipment in such a manner as to cause the accident to occur *so instantaneously* that the third officer was unable to warn anyone or prevent its happening." (See: *Mascuilli* case, 241 F. Supp. at 362.)

The Third Circuit affirmed the holding that the vessel was not unseaworthy solely on the basis of the

District Court's Finding No. 35 that the accident had been caused solely by the negligence of the stevedoring crew. (See *Mascuilli* case, 358 F. 2d at 133.)

The Supreme Court thereupon summarily reversed citing *Mahnich v. Southern SS. Company,* 321 U.S. 96, 64 S. Ct. 455, and *Crumady v. Joachim Hendrik Fisser,* 358 U.S. 423, 79 S. Ct. 445. (For other decisions reaching the same results see: *Alexander v. Bethlehem Steel Corporation,* 382 F. 2d 963, 1967 A.M.C. 2324; *Candiano v. Moore-McCormack Lines,* 382 F. 2d 961.)

It is submitted that the above authorities clearly substantiate the proposition that a longshoreman, while acting in the scope and course of his employment of discharging cargo from defendant's vessel, comes within the definition of "operational activity" and creates liability on the part of defendant vessel for injuries sustained by plaintiff seaman who also is working in the scope and course of his employment on board defendant's vessel.

B. THE PLAINTIFF, A SEAMAN IN THE EMPLOY OF DEFENDANT, WHILE ACTING IN THE COURSE AND SCOPE OF HIS EMPLOYMENT, HAD THE RIGHT TO RELY ON THE STEVEDORE PERFORMING HIS DUTY WITH CARE AND IS, THEREFORE, NOT CONTRIBUTORILY NEGLIGENT.

The trial court found:

> "12. At about 0830 on February 2, 1965, a supervisory employee of Matson Terminals, Inc. complained to libelant that the gantry crane was not

operating fast enough and requested libelant to remedy that situation. Pursuant to that request, libelant went to the operator's cab of the gantry crane (which was then occupied by Harry Johnson) and made adjustments which allowed the gantry crane to move athwartship at a faster speed.

"13. After libelant made the necessary adjustments to allow the gantry crane to move faster, he stood behind Harry Johnson, inside the cab, and observed the gantry crane operation. Libelant then thought he noticed that an electrical cable leading to the spreader apparatus of the gantry crane had become disengaged from its reel and he told Johnson, the gantry crane operator, that he wanted to inspect the electrical cable and Johnson brought the gantry crane to a stop in response to libelant's request.

"14. After waiting for the crane operator, Harry Johnson, to stop the crane, libelant then proceeded to the steel mesh platform outside the operator's cab. At that time the safety screen was at its starboardmost position, which allowed the gantry crane to operate. In order to inspect the electrical cable reel, libelant, by placing his feet on the second rung of the ladder leading to the platform and craning his head outside and atop the safety screen, was able to and did put his head into the space outside the screen, without placing the safety screen in the non-operative position and shutting off the power. Libelant assumed the operator of the gantry crane would not operate the crane while libelant was in a position of danger. While libelant had his head outside the safety screen, the gantry crane opera-

> tor started the gantry crane and libelant's head was caught and injured between the outboard portion of the safety screen and a stationary overhead object which came into contact with libelant's head because of the movement of the gantry crane."

In the Reporter's Transcript dated March 15, 1967 it is shown that plaintiff testified he would not have placed himself in this position had he known the crane was going to operate and the court agreed. (R.T. 19:2-11.)

The court also agreed that plaintiff never expected that the operator "would be stupid enough to start the equipment" (the court's choice of words) while plaintiff was in this position. (R.T. 33:16-22.)

The evidence also shows that plaintiff placed himself in this position only for a few seconds (R.T. 39:7-8) and it was in this few seconds that the crane was negligently operated by the crane operator.

The court also noted its complete acceptance of the plaintiff's testimony and that the only issue involved was a question of law. (R.T. 43:14-25.)

The trial court erroneously made the following conclusions:

> "1. That plaintiff's conduct, which might be argued to constitute assumption of risk, did constitute instead negligence.
>
> "2. That a seaman can be negligent for assuming that the defendant, through its agents, will exercise proper care for his safety until notified to the contrary."

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The trial court erroneously made the following conclusions:

"1. That plaintiff's conduct, which might be argued to constitute assumption of risk, did constitute instead negligence.

"2. That a seaman can be negligent for assuming that the defendant, through its agents, will exercise proper care for his safety until notified to the contrary."

It is submitted that plaintiff's conduct did not constitute negligence and that the plaintiff is under no duty to exercise care to discover extraordinary dangers that may arise from the negligence of the employer or those for whose conduct the employer is responsible, but the plaintiff may assume that the employer or his agent has exercised proper care for his safety until notified to the contrary and that plaintiff cannot be held to be negligent when making that assumption.

There is a danger of confusing the defenses of assumption of risk and contributory negligence and this danger was very aptly set forth by Justice Holmes in the case of *Schlemmer v. Buffalo R & T Railroad Company,* 205 U.S. 1, 27 S. Ct. 407. Therein the court stated:

> "Assumption of risk in this broad sense obviously shades into negligence as commonly understood. Negligence consists of conduct which common experience *with a special knowledge of the actor* shows to be *so likely to produce the result complained of, under the circumstances known to the actor,* that he is held answerable for that result, although it was not certain, intended, or foreseen. He is held to assume the risk upon the same ground. . . . But the difference between the two is one of degree rather than of time; and when a statute exonerates a servant from the former (assumption of the risk), if at the same time it leaves a defense of contributory negligence still open to the master (a matter upon which we express no opinion), then, unless great care be taken, the servant's rights will be sacrificed by

simply charging him with assumption of risk under another name." (27 S. Ct. 407 at 409.)

In the case at bar the evidence is uncontradicted that the plaintiff, Shaffer C. Tim, advised the operator of the crane that he was going to place himself in a situation where danger existed and communicated a desire to the operator that he bring the crane to a halt in order to allow plaintiff to perform his job. The evidence is also uncontradicted that the plaintiff waited until the operator did bring the crane to a stop in response to plaintiff's request and only then did he proceed to the platform to observe the spreader reel.

Under such circumstances the law is clear that the plaintiff, Shaffer C. Tim, was under no duty to exercise care to discover extraordinary dangers that may arise from the negligence of the shipowner or those for whose conduct the shipowner is responsible, but that the plaintiff may assume that the employer or his agent have exercised proper care for his safety until notified to the contrary. (See: *The Norland,* 101 F. 2d 967 at 974. See also: *Aivaliotis v. SS. Atlantic Glory,* 214 F. Supp. 568 at 574.)

This same proposition has been recognized by the United States Supreme Court *(Chesapeake v. De Atley,* 241 U.S. 310, 36 S. Ct. 564 at 567) and the Fifth Circuit Court of Appeals in *Ballard v. Atchison, Topeka and Santa Fe Railway Company,* 100 F. 2d 162 at 164. (For similar holdings in state courts see: *Crowder v. Atchison, Topeka and Santa Fe Rail-*

way, 117 Cal. App. 2d 68; *Murphy v. St. Claire Brewing Company,* 41 Cal. App. 2d 535; *Clark v. State of California,* 99 Cal. App. 2d 616; *Cooper v. Lunsford,* 234 Cal. App. 2d 554.) In these decisions the court pointed out that the injured plaintiff, under the Federal Employers Liability Act, had the right to presume that the negligent employee of the railroad involved would do his duty and that under such circumstances the plaintiff could not be considered to have also been negligent for presuming the defendant's employee would do his duty.

To allow each seaman to rely on the fact that other shipboard employees are not going to be negligent and will properly perform their duty is not only a practical rule but one of necessity. If, in fact, the seaman cannot rely on other shipboard employees to perform their duty properly, a ship could not either efficiently, or in a practical, manner, be operated.

The plaintiff, in the case at bar, might have been held negligent if he had gone to the platform *without first advising the operator* and thus merely hoped that the operator would not reactivate the crane before the plaintiff was finished with his job. But this type of negligent conduct was not, in fact, performed by the plaintiff. On the contrary, the plaintiff took great care to advise the operator of his proposed actions and even then did not move until the operator, in fact, brought the crane to a halt in response to the plaintiff's request.

It is submitted that the authorities set forth above clearly substantiate the proposition that the plaintiff

here cannot be held negligent for exercising his right to assume that defendant's agent will conduct himself in a safe manner and thereby perform his duty. It is submitted that it is incongruous to hold that by exercising a right plaintiff can, in any degree, be negligent. This is especially true in view of the fact as set forth above that the court concluded that plaintiff would not have placed himself in the position he did had he known the crane was going to operate and that plaintiff, *in fact,* never expected the crane operator to "be stupid enough to start the equipment". In other words, in view of these conclusions drawn by the court and the authorities set forth above (see: *Schlemmer v. Buffalo R & T Railroad Company,* supra) the plaintiff did not have any "special knowledge" that showed his conduct would "be so likely to produce the result complained of" or that the circumstances were "known to" the plaintiff.

C. THE TRIAL JUDGE, AS A TRIER OF FACT, CANNOT MAKE A FINDING ON DAMAGES AFTER HAVING ONCE FIRST CONCLUDED THERE IS NO LIABILITY ON THE PART OF DEFENDANT.

The court made one finding as to damages. In Finding No. 26 the court found:

> "The damages suffered by libelant, after applying the rule of maritime comparative negligence, would be $7,500.00, if respondent were legally responsible therefor."

The court failed to make any finding as to what injuries were sustained by the plaintiff nor the

amount of wage loss sustained by the plaintiff, including past and future wage loss.

That is to say that the trial court failed to make any finding on the issue of "nature and extent of injuries" that was set forth in the pre-trial order filed in this matter.

Furthermore, plaintiff in this action requested the following conclusion of law:

> "No. 9: Libelant had the right to rely on Harry Johnson, an employee of Matson Terminals, Inc., to perform his stevedoring duties in a non-negligent and safe manner."

The trial court failed to make a conclusion of law relative to this issue.

Rule 52(a) of the Federal Rules of Civil Procedure provides that the trial court, as a trier of fact, shall make findings of fact. The purpose of findings of fact is to enable the appellate courts to perform their function of promoting justice on the facts of each case as well as to establish general uniformity in law and Rule 52(a) utilizes the former and more complete equity review of both law and fact for all court actions. (See: *Moore's Manual, Federal Practice and Procedures,* page 1682, and authorities cited therein.)

The trial court's conclusion that the damages suffered by the plaintiff in this action amounted to $7,500.00, coupled with its failure to make any findings of fact or conclusions of law relative to the nature and extent of injuries sustained, deprives this appellate court of its reviewing power to consider whether the court's findings on the facts relative to

nature and extent of injuries substantiates the court's findings on damages in the amount of \$7,500.00. Consequently, this reviewing court and appellant are left with the conclusion that appellant sustained damages in the amount of \$7,500.00 but appellant and this court are denied the opportunity to determine whether these damages were based on the wages lost by appellant, whether the damages included a loss for both past and future wage loss, whether the damages were based solely on a conclusion by the court that no damages were lost and the damages were based solely on pain and suffering sustained by the appellant.

However, more significantly, the trial court erred in exceeding its power, as trier of fact, in drawing any conclusions or making any findings on the question of damages. Certainly it is clear that if the case had been tried before a jury the jury would be precluded in making any findings relative to damages after it first once concluded that the defendant was not liable. Rule 52(a) of the Federal Rules of Civil Procedure does not contemplate the trier of fact, when it is the court, to exercise powers as trier of fact in excess of those powers granted to a jury.

This concept was very aptly discussed in the case of *Sonken-Galamba Corporation, et al. v. Atchison, Topeka and Santa Fe Railway Company,* 34 F. Supp. 15 at page 16 wherein the court stated:

> "The theories which prompted the filing of this motion were not only that the findings of fact and conclusions of law which the court made

were erroneous, but the theory that a trial court, when trying a case at law in which a jury has not been demanded, not only should make such findings of fact as will support the judgment reached, but also should make such findings of facts as will fully present to any reviewing court every possible view of the case presented by plaintiff's petition and evidence, so that the reviewing court might have before it sufficient facts found by the trial court to support a judgment for the party other than the party to which the trial court has given judgment. To illustrate very simply, the theory is that if a suit for damages for personal injuries is tried to a trial court without a jury and the trial court finds that the defendant was not negligent and, therefore, that the plaintiff is not entitled to recover damages, the trial court also should find that, if the defendant was negligent, the plaintiff has been damaged in the amount of $5,000.00.

"With all respect for learned counsel, who have presented their views in this and all other connections with superb ability, I cannot subscribe to nor adopt this theory. While nothing of the kind was intended by counsel, the theory is degrading to a trial court. A United States District Court's judge, though the humblest in rank in Federal judicial hierarchy, occupies an honorable position. He is not a mere special master taking testimony for the benefit of some other court and, being a mere special master, making findings on every theory involved in the case. He is not a mere referee. He is something more than a 'whistling post' on the highway to an ultimate destination. His court is the court in which the case is to be decided and judgment pronounced,

subject only to possible review for errors committed. It is entirely inconsistent with such a view of the trial court that the judge thereof, having found the facts which, in his opinion, support the judgment reached, should proceed to make wholly superfluous and immaterial findings.

"It seems to me that the trial court should make only such findings of fact and state only such conclusions of law which are contemplated by Rule 52, Rules of Civil Procedure for District Courts, 28 U.S.C.A. following section 723c. That rule provides that 'in all actions tried upon the facts without a jury, the court shall find the facts specially and state separately its conclusions of law and direct the entry of the appropriate judgment'.

"I consider that this rule does not contemplate that there shall be findings of fact wholly inappropriate to the judgment entered and necessarily discarded, as unproved or immaterial, in connection with the conclusions of law reached. The facts to be found are the ultimate facts established by the evidence and supporting judgment."

It is submitted that the trial court exceeded the scope of its authority as the trier of fact on the issue of plaintiff's damages and then compounded such error by failing to make proper findings on the damage issue.

The trial court's action in this regard creates an impossible situation. The appellant is deprived of the opportunity to argue to this court that the trial court's conclusions on damages are, in fact, unsubstantiated by the evidence because neither appellant

nor this court can ascertain from the findings below what evidence and what facts the court used to come to its conclusion on the damage issue.

Furthermore, the trial court's finding that plaintiff was fifty per cent contributorily negligent is also erroneous without a basis in fact or in law upon which the court could make such a conclusion on this appeal. The entire issue of damages necessarily is an open question on this appeal and, if the plaintiff is successful on the liability issue then the damage issue should be presented to the new trier of fact in its entirety. To hold otherwise presents the following questions to this court:

If this court concludes that the plaintiff was not contributorily negligent for exercising his right to rely on the stevedore performing his duty in a non-negligent manner, then does the appellate court as a matter of law (in view of the trial court's conclusion that damages amounted to $7,500.00) direct that judgment be entered in the amount of $15,000.00? If not, then does the appellate court direct that judgment be entered in favor of the plaintiff, but that the issue of damages be retried, but that the damages cannot be in excess of $7,500.00 or $15,000.00?

It is because of this dilemma that the very purpose of Rule 52(a), as discussed in the authorities set forth above, is to confine the trier of fact to the issue of liability first and that in the event the trier of fact concludes defendant is not liable, that no findings and no conclusions should be made on the question of damages.

III

CONCLUSION

It is submitted that the above authorities require that the decision of the trial court below be reversed with direction that judgment in favor of plaintiff should be entered on the question of liability of the defendant without deduction for contributory negligence, and that this cause should be remanded for a new trial solely on the question of the nature and extent of the injuries and damages sustained by the plaintiff.

Dated, San Francisco, California,
March 11, 1968.

Respectfully submitted,
JARVIS, MILLER & STENDER,
HUGH B. MILLER,
R. JAY ENGEL,
Attorneys for Appellant.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

R. JAY ENGEL,
Attorney for Appellant.

No. 22,395

IN THE

United States Court of Appeals

For the Ninth Circuit

SHAFFER C. TIM, *Appellant,* vs. AMERICAN PRESIDENT LINES, LTD., a corporation, *Appellee.*	

Appeal from an Admiralty Decree of the United States District Court for the Northern District of California
Honorable Lloyd H. Burke, District Judge

APPELLEE'S BRIEF

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IN THE

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APPELLEE'S BRIEF

JURISDICTION

Jurisdiction of this Court exists, under 28 U.S.C. §1291, by virtue of a Notice of Appeal (R. 1, p. 92)[1] filed October 9, 1967, from a Final Decree (R. 1, p. 112) in admiralty entered in the United States District Court for the Northern District of California on October 5, 1967.

The District Court had jurisdiction, under 28 U.S.C. §1333, by virtue of a Libel (R. 1, p. 1) for damages,

[1]The record in this case consists of four volumes, not consecutively paginated. The references to both the pleadings and the oral evidence, therefore, are by volume number and page number, e.g., "R. 2, p. 75." Exhibits are referred to by letters, e.g., "Ex. A."

under the Jones Act (46 U.S.C. §688) and the General Maritime Law.

STATEMENT OF THE CASE

Appellant Shaffer C. Tim commenced this action by filing a Libel (R. 1, p. 1) against his former employer, American President Lines, Ltd., for damages on account of an injury, claiming that it resulted from negligence of Appellee and unseaworthiness of Appellee's vessel, the SS PRESIDENT TYLER, on which Tim was then serving as a seaman. The injury was found to have been caused by the concurrent negligence of Tim and a longshoreman-employee of a stevedore company employed by the United States and on board under its contract with the Government to handle the Government's cargo. The District Court found that the vessel and her appurtenances were seaworthy, that the stevedore was not an agent of the vessel owner, American President Lines, Ltd., and that American President Lines, Ltd. had not been negligent.

The underlying facts may be stated largely by quoting from the findings of the District Court.[2]

> "2. Libelant Shaffer C. Tim was employed by respondent as a seaman aboard the SS PRESIDENT TYLER in the capacity of chief electrician, from January 26 until February 2, 1965, when he suffered an accident in the course and scope of his employment.

---

[2]The complete Findings of Fact and Conclusions of Law are printed in Appendix "A" to this brief.

"3. At about 0900 on February 2, 1965, cargo at the No. 4 hatch of the SS PRESIDENT TYLER was being worked by employees of Matson Terminals, Inc. The loading and unloading of the cargo then aboard the SS PRESIDENT TYLER was done pursuant to a contract between the United States Government and American President Lines (MSTS Contract with American President Lines No. 48 dated July 1, 1950) and pursuant to a contract between the Procurement Division, U.S. Army Terminal Command, PAC, a branch of the United States Government, and Matson Terminals, Inc. (#DA-04-197-AMC-215(m)) effective July 1, 1964, and the terms of these contracts governed responsibilities as to the loading and unloading of the cargo. These contracts were not regarded by the trial judge as having significance insofar as the judgment reached was concerned.

"4. Respondent American President Lines did not select Matson Terminals, Inc. to load or unload the cargo aboard the SS PRESIDENT TYLER on February 2, 1965, had no oral or written contract with Matson Terminals, Inc. to do so and was not shown to have any ownership or other financial interest in Matson Terminals, Inc.

"5. Matson Terminals, Inc. was not the agent of American President Lines within the meaning of the common law agency concept or of 45 U.S.C. §51, as interpreted by the Supreme Court cases of *Sinkler v. Missouri Pacific Railroad Co.,* 356 U.S. 326 (1958) and *Hopson v. Texaco,* 383 U.S. 262 (1966), and was therefore not performing operational activities of the respondent at the time of the accident.

"6. The cargo was being worked by use of a mechanical apparatus known as a gantry crane. The

gantry crane was operated from a cab mounted upon the crane, about 30 feet above the weather deck and over the No. 4 hatch. The 'operating unit' relevant to this action consisted of the operator's cab, the controls to operate the crane inside the cab, a steel mesh platform to starboard and outside of the operator's cab and a safety screen which, when in the 'non-operating' position, lay over the top of the operator's cab and, when in the 'operating position,' extended over the platform outside the operator's cab. In order to enter the operator's cab, it was necessary to descend four steps, each step consisting of one horizontal steel bar, to reach the steel mesh platform. Once on the steel mesh platform, one would turn left and enter through a door to the operator's cab, which was approximately five feet square. Inside the operator's cab were the controls of the gantry crane and a chair which faced forward, from which the gantry crane operator would operate the gantry crane unit."

* * * * *

"8. The gantry crane operator's cab had a safety screen over the top of it, which, if extended to its starboardmost position, engaged an electrical circuit which energized the gantry crane and allowed it to operate. When the safety screen was moved about two to three inches to port from its 'operating position,' the electrical circuit was de-energized and the gantry crane unit would not operate. Libelant knew how to operate the gantry crane and knew the movement of the safety screen would render the gantry crane inoperative."

* * * * *

"10. The safety screen was of sufficient size to preclude an individual standing on the steel mesh

platform from raising his head above the screen vertically, that is, in a direct line perpendicular to the steel mesh platform."

* * * * *

"12. At about 0830 on February 2, 1964, a supervisory employee of Matson Terminals, Inc. complained to libelant that the gantry crane was not operating fast enough and requested libelant to remedy that situation. Pursuant to that request, libelant went to the operator's cab of the gantry crane (which was then occupied by Harry Johnson) and made adjustments which allowed the gantry crane to move athwartship at a faster speed.

"13. After libelant made the necessary adjustments to allow the gantry crane to move faster, he stood behind Harry Johnson, inside the cab, and observed the gantry crane operation. Libelant then thought he noticed that an electrical cable leading to the spreader apparatus of the gantry crane had become disengaged from its reel and he told Johnson, the gantry crane operator, that he wanted to inspect the electrical cable and Johnson brought the gantry crane to a stop in response to libelant's request.

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operative position and shutting off the power. Libelant assumed the operator of the gantry crane would not operate the crane while libelant was in a position of danger. While libelant had his head outside the safety screen, the gantry crane operator started the gantry crane and libelant's head was caught and injured between the outboard portion of the safety screen and a stationary overhead object which came into contact with libelant's head because of the movement of the gantry crane.[3]

"15. At all material times the gantry crane was operated by Harry Johnson, an employee of Matson Terminals, Inc."

* * * * *

"18. At the time of libelant's accident, the gantry crane, including the safety screen above the steel mesh platform, was in good working order and reasonably fit for its intended use.

"19. It was not negligent for libelant to be on the steel mesh platform when the crane was in the operative position, nor was it negligent for the crane operator to operate the crane when libelant was on the steel mesh platform.

"20. At the time of his accident, libelant knew that he could have moved the safety screen to the 'non-operating position' in a matter of several seconds and knew that he had the right to do so, but did not do so. Libelant further knew that, had he done so, the gantry crane unit would have been inoperative. Libelant was negligent in failing to move the

[3]Finding 14 did not include a determination that the plaintiff "relied on . . . the operator of the gantry crane" not to operate the crane, as stated in Appellant's Brief, p. 5.

safety screen to the 'non-operating position' before he placed his head outside the safety screen."

* * * * *

The District Court heard the testimony of all witnesses in open court and, after argument, announced its decision that the Appellant had failed to establish unseaworthiness or negligence of American President Lines and that the injury was the result of the joint and equal negligence of the Appellant and the stevedore employee operating the crane, and entered Findings of Fact and Conclusions of Law and Decree accordingly.

This appeal raises principally the question of whether the District Court's findings that Appellee's vessel was seaworthy and that Matson Terminals, Inc. was not an agent of the Appellee, based on substantial, convincing evidence in the District Court, should be overturned. Appellant also raises questions about the finding of contributory negligence and the amount of potentially recoverable damages. These questions would only arise in the event of a reversal of the decision below.

SUMMARY OF ARGUMENT

The findings in this case, as in other civil cases, are subject to the "clearly erroneous" rule and therefore are to be affirmed unless the evidence leads to a definite and firm conviction that error has been committed. The evidence in this case does not support—much less compel—findings for Appellant and fully supports the District Court's findings.

This Court has consistently held that negligence of longshoremen employees of an independent stevedore is not imputed to the shipowner and that a longshoreman's negligent act at the moment of injury will not cause a vessel to be unseaworthy. *Billeci v. United States,* 298 F. 2d 703, 1962 A.M.C. 826 (9th Cir. 1962) and *Titus v. The Santorini,* 258 F. 2d 352, 1959 A.M.C. 1042 (9th Cir. 1958). Moreover, this Court has denied recovery to injured longshoremen in circumstances in which the injured party failed to utilize known safety precautions. *Larsson v. Coastwise (Pacific Far East) Line,* 181 F. 2d 6, 1950 A.M.C. 769 (9th Cir. 1950)

The evidence clearly indicated that Matson Terminals, Inc. was not the "agent" of American President Lines, at common law or within the interpretation of 45 U.S.C. §51, as enunciated by *Hopson v. Texaco, Inc.,* 383 U.S. 262, 1966 A.M.C. 28 (1966) and *Sinkler v. Missouri Pacific Railroad Co.,* 356 U.S. 326 (1958). Unlike the parties in those cases, American President Lines was under no contractual relationship with Matson Terminals, Inc. and did not, in fact, choose Matson Terminals, Inc. to perform the unloading duties. Matson Terminals, Inc. was performing its operations pursuant to a contract with the United States Government and unloading the Government's cargo as the Government's contractor and subject to the Government's direction. Furthermore, the concept of the Federal Employers' Liability Act that a railroad is a unitary enterprise is not applicable here, as the Supreme Court, in *Reed v. Steamship Yaka,* 373 U.S. 410, 1963 A.M.C. 1373 (1963), has refused to accept the view that a stevedore and a shipowner are engaged in a uni-

tary enterprise. The cases which Appellant cites in support of his "agency" contention have consistently involved a contractual relationship between the "agent" and the railroad defendant.

The Appellant's claim of unseaworthiness involves a contention that this Court should make a radical change in the doctrine of seaworthiness so that it would no longer be possible to make a fact finding that the vessel was seaworthy in the event of injury through a longshoreman's negligence. Such a contention is contrary to long-established and specific doctrine and involves placing an unwarranted and strained construction upon a *per curiam* order of the Supreme Court.

The finding that Appellant was contributorily negligent in failing to use a safety screen, supplied to prevent the type of injury which he incurred, was supported by substantial evidence and the lower court's propriety in assessing damages without a finding of liability is clearly supported by case law. In any event, the issues dealing with contributory negligence and damages need not be reached in this appeal.

ARGUMENT

I. THE FINDINGS ARE TO BE UPHELD UNLESS CLEARLY ERRONEOUS.

This is an appeal attacking the District Court's Findings of Fact. In an admiralty appeal, such as this, the standard of review of Findings of Fact is the same as in other civil cases under Rule 52, F.R.C.P. *McAllister v.*

United States, 348 U.S. 19, 1954 A.M.C. 1999 (1954). Rule 52 provides, in part, as follows:

> "Rule 52. Findings by the Court. (a) Effect . . . Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses . . ."

Determinations with respect to negligence,[4] seaworthiness[5] and agency relationships[6] are findings of fact falling within this rule.

II. THE NEGLIGENCE OF AN EMPLOYEE OF MATSON TERMINALS, INC. IS NOT IMPUTED TO AMERICAN PRESIDENT LINES SO AS TO MAKE AMERICAN PRESIDENT LINES LIABLE FOR NEGLIGENCE.

In this Circuit it has been consistently held that negligence of a longshoreman employed by the contract stevedore is not imputable to the shipowner. In *Billeci v. United States,* 298 F. 2d 703, 1962 A.M.C. 826 (9th Cir. 1962), a longshoreman was injured when struck by a hatch cover which was caused to fall due to the negligent conduct of a fellow longshoreman. The negligent act of the fellow longshoreman was his failure to use a locking safety device which would have kept the winch from falling out of gear and, had either one of two safety devices

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[4]*Pacific Tow Boat Company v. States Marine Corp.,* 276 F. 2d 745, 752, 1960 A.M.C. 696, 705 (9th Cir. 1960).

[5]*Mahnich v. Southern Steamship Co.,* 321 U.S. 96, 98, 1944 A.M.C. 1, 3 (1944); *Luckenbach v. McCahan Sugar Refining Co.,* 248 U.S. 139, 145 (1918).

[6]*Pacific Can Co. v. Hewes,* 95 F. 2d 42, 46 (9th Cir. 1938); *Mitton v. Granite State Fire Insurance Co.,* 196 F. 2d 988, 990 (10th Cir. 1952).

available to the winch operator, been used, the accident would have been prevented.

The libelant sued for unseaworthiness and *negligence*. The District Court, in its opinion following trial, held that the negligent operation of a seaworthy appliance by the stevedore could not create liability on the shipowner and took notice of the contention that the negligence of the stevedore should be imputed to the shipowner, but refused to do so. 185 F. Supp. 711, 715, 1961 A.M.C. 111, 117.

Agreeing that, "plaintiff's injury was sustained by the negligent *use* of a seaworthy appliance at the very moment of injury," and "that the winch and its appurtenances were seaworthy and reasonably fit for their intended use and that libelant's injuries were directly and solely caused by a fellow longshoreman's negligent operation of the winch," this Court affirmed. 298 F. 2d at 706-7, 1962 A.M.C. at 830.

In *Titus v. The Santorini,* 258 F. 2d 352, 1959 A.M.C. 1042 (9th Cir. 1958), Judge Chambers posed a situation similar to that presented in the instant case. In discussing why a rope broke, Judge Chambers considered four possibilities. In connection with the third possibility he stated:

> "Third, there was the possibility the winch was improperly operated or the loading was improperly done by a fellow longshoreman at the instant when the breaking occurred. In this field, the outlawed practice of winch operators 'tightlining' their cables and producing an unusual strain on the wires and lines is the most typical. But there are others. There was no direct evidence that the loading was conducted

> in any way but in a skillful manner. *But if the causation of the break was in the third category, negligence at the moment of a fellow longshoreman, the ship would not be liable.*" (Emphasis added.) 258 F. 2d at 353, 1959 A.M.C. at 1044.

In *Larsson v. Coastwise (Pacific Far East) Line,* 181 F. 2d 6, 1950 A.M.C. 769 (9th Cir. 1950), Larsson, a seaman, was injured while he was oiling a winch which was negligently thrown into operation by a longshoreman. The appellant (Larsson) contended that the ship was unseaworthy and that the shipowner was liable for damages caused by, among other things, the negligence of the winch driver who commenced operation of the winch while appellant was oiling it. As in the present case, the appellant's own negligence in failing to make use of safety devices provided concurred with the negligence of the longshoreman to produce the injury. This Court stated:

> "The crucial fact in the case, however, is that each winch on the ship was equipped with a shut-off valve; that the oiler, by means of the valve, could close and cut off the steam to the winch; and that by cutting off the steam, the winch would be rendered immovable and absolutely safe to everyone. It is the contention of the appellee, therefore, that the injury to appellant resulted from his failure to use the simple safety precaution of cutting off the steam from the winch valve before proceeding to oil the winch." 181 F. 2d at 8, 1950 A.M.C. at 771.

This Court upheld the shipowner's contention and affirmed the decision.

III. THE DISTRICT COURT'S FINDING THAT MATSON TERMINALS, INC. WAS NOT THE "AGENT" OF AMERICAN PRESIDENT LINES WAS FULLY SUPPORTED BY THE EVIDENCE IN ACCORDANCE WITH APPLICABLE LEGAL STANDARDS.

The United States Government and American President Lines agreed by contract that all cargo would be loaded by the government at any dock or wharf that the government may direct. The government was to pay all stevedoring expenses and any damage done by the act or neglect in performing the government's duties of loading and discharging the vessel was to be repaired at the government's expense.[7]

The United States Government and Matson Terminals, Inc. agreed by contract that Matson Terminals, Inc. would perform all stevedoring services at Oakland Army Terminal and the government would provide Matson Terminals, Inc., among other things, the names of the vessels booked for cargo, the bills of lading and a cargo stowage plan. Matson Terminals, Inc. was responsible for the work area upkeep and was liable to the government for bodily injury occasioned in whole or in part by Matson Terminals' negligence.[8]

The definition of the word "agent" as used in the Federal Employers' Liability Act, 45 U.S.C. §51, has been interpreted by the Supreme Court in *Hopson v. Texaco, Inc.*, 383 U.S. 262, 1966 A.M.C. 281 (1966), as follows,

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[7]Contract No. MST-48 Article 5, Sections A, B, F, G; Appellee's exhibit in evidence, which by stipulation will be marked "F".

[8]Contract No. DA-04-197 AMC 215(n), Section 1 (A), (D), (N), Section III GP (32)(A)(3); Appellee's exhibit in evidence which by stipulation will be marked "E".

quoting *Sinkler v. Missouri Pacific Railroad Co.,* 356 U.S. 326 (1958):

> "In order to give 'an accommodating scope . . . to the word "agents", . . . we concluded that when [an] . . . employee's injury is caused in whole or in part by the fault of others performing, *under contract,* operational activities of the employer, such others are "agents" of the employer within the meaning of Section 1 of F.E.L.A.' " (Emphasis added.) 383 U.S. at 264, 1966 A.M.C. at 283.

Matson Terminals, Inc., was found, upon very clear evidence, not to come within this definition. Based on uncontradicted evidence, which Appellant does not challenge, the trial court found:

> "Respondent, American President Lines did not select Matson Terminals, Inc. to load or unload the cargo aboard the SS PRESIDENT TYLER on February 2, 1965, had no oral or written contract with Matson Terminals, Inc. to do so and was not shown to have any ownership or other financial interest in Matson Terminals, Inc." (Finding of Fact No. 4, Appendix "A")

The Supreme Court emphasized in *Hopson:*

> "And it was respondent—not the seamen—which selected, as it had done many times before, the taxi service. Respondent—the law says—should bear the responsibility for the negligence of the driver which it chose." 383 U.S. at 264, 1966 A.M.C. at 283.

American President Lines did not select Matson Terminals, Inc. to load the cargo which was being loaded aboard the SS PRESIDENT TYLER at the time of

Appellant's accident (Finding of Fact No. 4, Appendix "A"). Matson Terminals, Inc. had contracted with the United States Government to do this work aboard Appellee's vessel and at the time of Appellant's accident Matson Terminals, Inc. was performing services for the United States Government, the owners of the cargo, and not for Appellee or the vessel (Finding of Fact No. 4, Appendix "A").

In *Sinkler, supra,* the petitioner was employed as a cook by the Missouri Pacific Railroad Company. He was injured through the negligence of a member of the switching crew employed by Belt Railway. The court found that Belt Railway was organized by several carriers, including respondent and, in fact, respondent owned one-half of the Belt Railway stock and respondent had designated one-half of Belt's board of directors. Furthermore, the jury, in response to a special interrogatory submitted by the trial judge, expressly found that the "Belt Railway 'submits itself to the right of control and supervision of the other [respondent Missouri Pacific Railroad] with respect to all the details of such work'." 356 U.S. at 328, footnote No. 2.

In deviating from the common law, which regards the torts of fellow servants as separate and distinct from the torts of the employer, the Court, in *Sinkler,* states:

> "[I]t was the conception of this legislation [FELA] that the railroad was a *unitary enterprise,* its economic resources obligated to bear the burden of all injuries befalling those engaged in the enterprise arising out of the fault of any other member engaged in the common endeavor." (Emphasis added.) 356 U.S. at 330.

The holding that a railroad switching company, half owned by the respondent, is the agent of the respondent for the purposes of 45 U.S.C. §51 (the F.E.L.A.), cannot support, much less require, a ruling that Matson Terminals, Inc., an independent contractor not hired or selected by Appellee and engaged in services for interests other than Appellee, i.e., the United States Government and the cargo owners, was the agent of Appellee.

As *Sinkler* emphasized, F.E.L.A. legislation was generated from the conception that the railroad was a unitary enterprise. By contrast with the F.E.L.A. legislative conception, it is distinctly the conception of the Longshoremen's and Harbor Workers' Act that the shipowner and stevedore are not a unitary enterprise. If this were not so—that is, if shipowner and stevedore actually were a unitary enterprise—the shipowner would have the benefit of immunity from suit under the Longshoremen's and Harbor Workers' Act and the third-party lawsuits in which the shipowner is presently sued by the longshoremen would be eliminated.

In the shipping industry, the stevedore and shipowner have separate interests and separate areas of control and they cannot be considered a unitary enterprise. Indeed, the Supreme Court has emphatically refused, in *Reed v. Steamship Yaka,* 373 U.S. 410, 1963 A.M.C. 1373 (1963), to accept the view that stevedore and shipowner are engaged in a unitary enterprise, but, on the contrary, held that, even when a single party performs both functions, it has two separate capacities and, while immune from suit in one capacity, is vulnerable in the other.

It is indeed noteworthy that decisions subsequent to *Sinkler* and *Hopson* in which an "agency" relationship was found, have all involved situations where there was a contractual agreement and arrangement between the employer of the injured party and the "agent." Appellant, unable to cite a case where this is not so, has offered *Carney v. Pittsburgh and Lake Erie Railroad Company*, 316 F. 2d 277 (3d Cir. 1963) and *Leek v. Baltimore and Ohio Railroad Company*, 200 F. Supp. 368 (N.D. W.Va. 1962) for the court's consideration of this question. In *Carney, supra*, the Pittsburgh and Lake Erie Railroad Company was held liable for the negligence of employees of Pittsburgh and Lake Erie Railroad Company Y.M.C.A., where employees of defendant, through agreement with the Y.M.C.A. (agent) were lodged. In the *Leek* case, *supra*, the employer (defendant) was held liable for the negligence of a taxicab company, where for several years the defendant had, by agreement and arrangement, selected the taxicab company to shuttle their train crews from point to point.

As the doctrine of the *Hopson* and *Sinkler* cases, on which Appellant relies, is grounded in the F.E.L.A. and decisions construing that Act, it is appropriate to look at other cases under the F.E.L.A. dealing with comparable situations.

In *Gaulden v. Southern Pacific Company and Pacific Fruit Express Company*, 174 F. 2d 1022 (9th Cir. 1949), this Court affirmed (on the opinion below), the District Court's decision[9] that Pacific Fruit Express Company

[9] *Gaulden v. Southern Pacific Company and Pacific Fruit Express Company*, 78 F. Supp. 651 (N.D.Cal. 1948).

was not an agent of Southern Pacific Company so as to make Southern Pacific liable, under the F.E.L.A., for negligence of Pacific Fruit in the course of its operation of unloading ice from a railroad car. This was so despite the fact that Pacific Fruit was owned 50% by Southern Pacific and engaged in owning and servicing refrigerated railroad cars and supplying them to Southern Pacific and other railroads under contract provisions which included a recital that services were performed "as the agent of the railroads." Despite the importance of these services and their connection with the railroad's activities in the carriage of fresh fruit, it was held, upon an analysis of the actual relations of the parties and the lack of control by Southern Pacific over the "manner and means" of performance, that no agency relationship existed.

Similarly, in *Del Vecchio v. The Pennsylvania Railroad Company,* 233 F. 2d 2 (3d Cir. 1956), it was contended that, for F.E.L.A. purposes, a company which contracted with the railroad to handle coal for it, unloading it from the railroad cars and loading it into vessels, was an agent of the railroad. As in the present case, there was no common ownership or control of the companies involved and the railroad did not supervise the manner of performance, although it did, in contrast to Appellee's role here, designate the particular cargo to be handled and where it should be delivered. The Court of Appeals emphatically affirmed the finding of the District Court that the contractor was an independent contractor and not an agent. In the present case not even the contractual relationship found in *Del Vecchio* existed between the carrier and the loading stevedore.

As Appellant himself points out (Brief, p. 9), the underlying rationale of *Sinkler v. Missouri Pacific Railroad Company, supra,* was stated as follows:

> "It was the conception of this legislation [F.E.L.A.] that the railroad was a unitary enterprise, its economic resources obligated to bear the burden of all injuries befalling those engaged in the enterprise *arising out of the fault of any other member engaged in the common endeavor.*" (Emphasis added.) 356 U.S. at 330.

Appellant's contention is that the court below was compelled to find, in effect, that the stevedore's activities constituted part of the "common endeavor," making it a part of a "unitary enterprise" with the shipowner. But the cases already cited, along with other F.E.L.A. cases, show that the concept stated in *Sinkler* is by no means so broad as Appellant contends. The latest of these cases is *Edwards v. Pacific Fruit Express Company,* ...... U.S. ......, 36 L. W. 4291 (1968), where the attempt was to hold Pacific Fruit Express, under the F.E.L.A., as a common carrier by railroad. An unanimous Court, after outlining the functions of the Company (already described in the *Gaulden* case, *supra,* which it cited and followed) referred to previous decisions illustrating "the rationale that there exist a number of activities and facilities which, while used in conjunction with railroads and closely related to railroading, are yet not railroading itself." 36 L. W. at 4292.

It is against this background that the expression "operational activities" must be read in the *Sinkler* and *Hopson* cases. In *Sinkler* the activity involved was the

movement of railroad cars. This was the very essence of railroading—the activity at the heart of the railroad's operation, without which it could hardly be said to be in the business. In *Hopson,* the activity was the performance of a duty directly imposed upon the shipowner by statute law and therefore, as a matter of law, a part of the shipowner's operations, rather than those of anyone else.

Nothing in the cases suggests or permits the extension of the "operational activities" of a railroad or shipowner to the activities of others, simply because they are connected with its functions or contribute to the transportation of goods by rail or sea. And certainly there is no basis for regarding as "operational activities" of the shipowner the activities of others which the shipowner not only has no legal duty to perform but has not agreed nor held itself out to its customers to perform, nor charged them for, and which are performed by the customer as a means of being able to take advantage of the service it has purchased from the shipowner, which consists, as in the present case, of making its vessels available at agreed rates to carry such cargo as the customer may choose to place on board.

IV. THE COURT'S FINDING OF SEAWORTHINESS WAS SUPPORTED BY SUBSTANTIAL EVIDENCE AND BY NO MEANS ERRONEOUS.

Appellant makes no claim that error exists in the District Court's findings with respect to the design and construction of the equipment involved in this case and does not claim that the equipment was not in good condition and reasonably fit for the purpose intended, and

points to no evidence to the contrary. In short, Appellant presents no contention at all that the vessel was not seaworthy according to the usual standards by which seaworthiness has been judged.

What Appellant does appear to contend is that a vessel not only may, but must, be found unseaworthy in the event that an accident occurs on board as the result of the negligence of a fellow worker and regardless of the creation of any intervening, dangerous and material condition as a result of such negligence. It requires no citation to remind this Court that it has had many occasions to affirm both findings of seaworthiness and findings of unseaworthiness. The court has repeatedly observed in connection with those cases that the finding of seaworthiness (reasonable fitness of the vessel and her appurtenances for the purpose intended) is a finding of fact which may ordinarily be determined either way by the trier of fact.

What the Appellant now proposes is to reverse the trial court's finding of seaworthiness by the introduction of two novel and revolutionary developments at once. *First,* he would have this Court hold that, without the existence of any unsafe condition antecedent to the injury, unseaworthiness might be found whenever a seaman or longshoreman is injured by the contemporaneous negligence of his fellow worker ("instantaneous unseaworthiness"). *Second,* he would have this Court hold that, when such contemporaneous negligence is discovered, the trier of fact does not have the choice which he has heretofore exercised in the more classic type of unseaworthiness case, but must resolve the issue in only one way, by finding the

vessel unseaworthy. If, as it is generally understood, the policy of the warranty of seaworthiness is to encourage the shipowner to supply and keep in order the proper appliances appurtenant to the ship for the safety of seamen and longshoremen,[10] it is difficult to see how the policy would be served by an extension of the doctrine to cases of contemporaneous negligence of a fellow workman. When the longshoreman assigned to work on the pier is there injured by the negligence of a fellow workman, in the use of equipment or otherwise, the longshoreman has only his workmen's compensation remedy. It is difficult to see why the position should be any different because he happens to be assigned to work aboard ship, if the negligence of the fellow workman has not created some defective vessel condition which itself becomes the cause of the injury.

Appellant bases his far-reaching contentions upon the reading of a *per curiam* opinion of the Supreme Court in *Mascuilli v. United States,* 387 U.S. 237, 1967 A.M.C. 1702 (1967), in which the court, without benefit of hearing, disposed of the matter by citing two prior decisions without comment. It is true that the Court of Appeals for the Second Circuit has read the *Mascuilli* case as Appellant does[11] but the reading is no less strained on that account. As Appellant recognizes (Brief p. 12), the question on *certiorari* was presented in terms of a "dangerous condition." The *Mascuilli* case involved the problem of the

[10]See *Mahnich v. Southern S. S. Co.,* 321 U.S. 96, 104, 1944 A.M.C. 1, 7 (1944).

[11]See *Candiano v. Moore-McCormack Lines,* 382 F. 2d 961, 1967 A.M.C. 2312 (2d Cir. 1967) cited on p. 13 of Appellant's Brief.

actual parting of a line which was part of the ship's rigging, as well as a problem concerning the proper setting of winch circuit breakers. When one considers that the two cases which the Supreme Court cited without comment in its *per curiam* concerned the parting of a line[12] and a problem of the proper setting of winch circuit breakers,[13] it is indulging in a high degree of speculation to assert that the real meaning of the order was to indicate a Supreme Court determination that a radical change should be made in the doctrine of seaworthiness[14] under which it would no longer be possible to find the vessel seaworthy in a case of negligence of a fellow longshoreman.

In *Fenton v. A/S Glittre,* 1967 A.M.C. 317 (E.D.N.Y. 1966), a winch operator (who was a co-worker of the plaintiff) was taking general cargo on board. When the plaintiff walked towards the cargo draft to steady it, the draft broke apart and, in attempting to remove himself from harm's way, the plaintiff was injured. The District Judge found that the stevedore, Atlantic Stevedoring Company, Inc., was in complete charge of the loading operation and that the shipowner supplied the longshoremen with a reasonably seaworthy ship, together with its gear, for the conduct of stevedoring operations. Concluding that the accident was caused solely by the negligence of the plaintiff *and his co-worker operating the winch,*

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[12]*Mahnich v. Southern S. S. Co.,* 321 U.S. 96, 1944 A.M.C. 1 (1944).

[13]*Crumady v. Joachim Hendrik Fisser,* 358 U.S. 423, 1959 A.M.C. 580 (1959).

[14]See discussion in *Jackson v. S. S. KINGS POINT,* 276 F. Supp. 451 (E.D.La. 1967).

the District Judge gave judgment to the shipowner and against the plaintiff. The Court of Appeals affirmed, *Fenton v. A/S Glittre,* 370 F.2d 146, 1967 A.M.C. 316 (2d Cir. 1966). The United States Supreme Court denied certiorari (387 U.S. 944). Appellee submits that, had the Supreme Court intended to hold in *Mascuilli* that every negligent act of a longshoreman must create an unseaworthy condition, then the *Fenton* case, two weeks later, would have afforded the Supreme Court the obvious opportunity to say so.

V. ALTHOUGH THE DISTRICT COURT'S FINDINGS ON THE DAMAGES ISSUES ARE NOT INVOLVED IN THE DECREE AND NEED NOT BE REACHED BY THIS COURT, THEY ARE APPROPRIATE IN ANY EVENT.

A. Appellant's Contributory Negligence Was Fully Supported by the Evidence and Would Require Reduction of Damages.

The trial judge found that at the time of Appellant's accident the safety screen above the platform upon which Appellant was standing was of sufficient size to preclude an individual standing on the steel mesh platform from raising his head above the screen vertically (Finding of Fact No. 10, Appendix "A"). At trial, Appellant testified that, when he left the operator's cab, he did not tell the crane operator that he was going to put his head outside the safety screen to inspect the electric cable. (R. 3, p. 31).[15]

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[15]"Q. Now, you didn't tell him how you were going to inspect it, did you?

A. No, I just—I told him I am going out.

Q. And you didn't tell him you were going to put your head outside the safety screen and inspect?

A. No."

A finding was also made that it was not negligent for Appellant to be on the steel mesh platform when the crane was operating and it was *not* negligent for the crane operator to operate the crane when Appellant was on the steel mesh platform (Finding of Fact No. 19, Appendix "A"). The gantry crane operator was found to be negligent because he operated the gantry crane when Appellant's head was outside the safety screen after Appellant had stood on the second rung of a ladder leading to the platform and craned his head outside and atop the safety screen (Findings of Fact Nos. 14 and 21; Appendix "A").

After hearing this evidence, the trial judge found that Appellant was negligent in the following manner:

> "At the time of his accident, libelant knew that he could have moved the safety screen to the 'non-operating position' in a matter of several seconds and knew that he had the right to do so, but did not do so. Libelant further knew that, had he done so, the gantry crane unit would have been inoperative. Libelant was negligent in failing to move the safety screen to the 'non-operating position' before he placed his head outside the safety screen." (Finding of Fact No. 20, Appendix "A").

Appellee submits that *Larsson v. Coastwise Line, supra,* following *Shields v. United States,* 175 F. 2d 743, 1949 A.M.C. 1355 (3d Cir. 1949), fully supports, if it does not compel, the finding by this Court that the seaman is to be held for negligence when he fails to use a safety device which would render it impossible for a longshoreman to negligently start the vessel's machinery.

Appellant's brief contends that the District Court erred in holding Appellant negligent because he had the right

to rely on the stevedore performing his duty with care. The cases which Appellant cites all deal with assumption of risk rather than contributory negligence. They conclude that it is not negligent for an employee to assume his employer will exercise due care toward him. The District Court did not conclude Appellant was negligent in assuming his employer would exercise due care, but rather found Appellant negligent because he did not exercise ordinary care in failing to move the safety screen which would de-energize the crane before he placed his head outside and above the safety screen.

Appellant's brief, on page 18, cites the case of *Murphy v. St. Claire Brewing Company,* 41 Cal. App. 2d 535, 107 P. 2d 273 (1940), in which the court affirms an instruction to the jury ". . . it is not negligence to assume that he is not exposed to danger . . . by such other person, *provided that such person himself uses reasonable care to protect his own safety.*" (Emphasis added) 107 P. 2d at 276.

The evidence is uncontradicted that instead of availing himself of a known safety device which had been placed on the gantry crane to prevent this type of accident (Finding of Fact No. 9, Appendix "A"), Appellant took it upon himself to crane his head around and atop the safety screen and that while so positioned he suffered the injuries of which he now complains.

B. The District Court Properly Made a Finding of Fact As to the Amount of Appellant's Damages.

After listening to all of Appellant's evidence on injuries and damages[16] the trial judge concluded that the damages suffered by Appellant amounted to $15,000, so that, after applying the maritime rule of comparative negligence, Appellant's recovery would be $7,500, if Appellee were legally responsible therefor (Finding of Fact No. 26, Appendix "A"). The trial judge also found:

> "The negligence of the gantry crane operator and the negligence of libelant were the sole proximate causes and combined equally to cause libelant's accident and injuries." (Finding of Fact No. 22, Appendix "A").

Appellant does not now assert that he has not had his day in court on the issues of injuries and damages nor that the trial judge did not listen to or fairly assess all the evidence that Appellant had to offer on these issues. Appellant contends, however, that the trial judge could not find on the issue of damages once he found that the Appellee was not liable.

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[16]The Appellant testified that he injured his left ear, right ear, left side of head, neck and shoulder, and that he went to the San Francisco Marine Hospital for 21 days. The trial judge personally inspected Appellant's physical condition and Appellant's hospital records were introduced into evidence. The trial judge heard that Appellant was not fit for sea duty from February 2 until May 17, 1965 and that Appellant claimed he could not work until August 1965, when he joined the JAPAN BEAR. Evidence that Appellant could earn $1,000 a month as chief electrician was presented by Appellant and Appellant's earnings records were introduced into evidence. Proof was made that Appellant was paid maintenance for his unfitness period from February 2 to May 17, 1965 and unearned wages of $1,120 from February 2 until March 25, 1965. The trial judge also learned that, at the time of trial, Appellant "felt all right" (R. 3, pp. 19-26).

It is true that perhaps the trial judge did not have to find on the issue of damages and a failure to do so would certainly not have been reversible error. It does not follow, however, that the District Court cannot make such findings on damages after all the evidence is presented on that issue. Judicial economy in deciding cases is served by having the trial court decide all possible fact issues and the procedure of assessing damages after a finding of no liability (in the event of reversal on the liability question) has been followed by many trial judges and evidently approved by this Court.[17]

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[17]In *Woodbury v. United States*, 232 F. Supp. 49, 59 (D.Ore. 1964), the trial judge, after finding no liability, stated:

> "Under ordinary circumstances, it would be beyond the scope of this opinion, and pure dictum, to pass on the question of damages. However, my findings and conclusions may not meet with the approval of the Court of Appeals. If the appellate court arrives at a different result, it might desire my views on the issue of damages."

The trial court then went on to find the amount that the government would be entitled to recover against the plaintiff if liability existed. The Court of Appeals reversed the trial judge's decision in part, but affirmed findings as to the amount of recovery. *United States v. Woodbury*, 359 F. 2d 370, 379 (9th Cir. 1966).

In *Neterer v. United States*, 183 F. Supp. 893, 1960 A.M.C. 1788 (D.Md. 1960), Judge Watkins found no liability on the part of the shipowner, but stated that, if required to determine damages, the court would fix damages at $7,500 and would find that libelant contributed to his own injuries to the extent of 75%.

In *Young v. United States*, 272 F. Supp. 738 (D.S.C. 1967), the trial judge, after finding that the court did not have jurisdiction, stated:

> "Nevertheless, in order to fully resolve the case after hearing the evidence, and in order to save a possible remand, I have also conditionally ruled on the merits even though I have determined the court has no jurisdiction." 272 F. Supp., at 743.

In *Gomez v. SS DOROTHY*, 183 F. Supp. 499, 1960 A.M.C. 82 (D.P.R. 1959), Judge Delehant stated:

> "The court has thus proceeded with its findings of fact to a determination respecting the damages by the libelant sus-

For cogent reasons of judicial economy, there is ample precedent for the propriety of the course taken by the judge below on the issue of damages. Indeed, like other findings of fact, those dealing with the subject of damages should stand unless clearly erroneous. *Waterman Steamship Corp. v. Rodriguez,* 290 F. 2d 175 (1st Cir. 1961).

CONCLUSION

For the foregoing reasons we submit that the Decree should be affirmed.

April 29, 1968.

Respectfully submitted,

LILLICK, MCHOSE, WHEAT, ADAMS & CHARLES,
GRAYDON S. STARING,
GARRETT P. GRAHAM,
Attorneys for Appellee.

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tained for which an award should be made, if it were assumed or found that he is entitled at all to recover against the respondents. That course has been thought to be appropriate in recognition of the possibility that it may ultimately be determined on appeal that the court is mistaken in the findings of fact now to be announced, and directly oriented to the legal responsibility to the libelant on the part of the respondents. The aggregate amount of the several items of damages thus found is $4,488.88." 183 F. Supp., at 507.

Judge Kilkenny, in *Tallmon v. Toko Kaium K. K. Kobe,* 278 F. Supp. 452 (D.Ore. 1967), held that the maximum recovery under the Oregon death statute, when applied to admiralty law, is $25,000, and announced that, since the Court of Appeals might take a different view, he believed the trier of facts in this case might well go forward and determine the amount of actual damages as if no such limitation existed.

Certificate of Counsel

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Garrett P. Graham,
Of Attorneys for Appellee.

(Appendix "A" Follows)

Appendix “A”

Appendix "A"

FINDINGS OF FACT

1. Respondent American President Lines, Ltd. owned and operated the SS PRESIDENT TYLER.

2. Libelant Shaffer C. Tim was employed by respondent as a seaman aboard the SS PRESIDENT TYLER in the capacity of chief electrician, from January 26 until February 2, 1965, when he suffered an accident in the course and scope of his employment.

3. At about 0900 on February 2, 1965, cargo at the No. 4 hatch of the SS PRESIDENT TYLER was being worked by employees of Matson Terminals, Inc. The loading and unloading of the cargo then aboard the SS PRESIDENT TYLER was done pursuant to a contract between the United States Government and American President Lines (MSTS Contract with American President Lines No. 48 dated July 1, 1950) and pursuant to a contract between the Procurement Division, U. S. Army Terminal Command, PAC, a branch of the United States Government, and Matson Terminals, Inc. (#DA-04-197-AMC-215(m)) effective July 1, 1964, and the terms of these contracts governed responsibilities as to the loading and unloading of the cargo. These contracts were not regarded by the trial judge as having significance insofar as the judgment reached was concerned.

4. Respondent American President Lines did not select Matson Terminals, Inc. to load or unload the cargo aboard the SS PRESIDENT TYLER on February 2, 1965, had

no oral or written contract with Matson Terminals, Inc. to do so and was not shown to have any ownership or other financial interest in Matson Terminals, Inc.

5. Matson Terminals, Inc. was not the agent of American President Lines within the meaning of the common law agency concept or of 45 U.S.C. §51, as interpreted by the Supreme Court cases of *Sinkler v. Missouri Pacific Railroad Co.,* 356 U. S. 326 (1958) and *Hopson v. Texaco,* 383 U. S. 262 (1966), and was therefore not performing operational activities of the respondent at the time of the accident.

6. The cargo was being worked by use of a mechanical apparatus known as a gantry crane. The gantry crane was operated from a cab mounted upon the crane, about 30 feet above the weather deck and over the No. 4 hatch. The "operating unit" relevant to this action consisted of the operator's cab, the controls to operate the crane inside the cab, a steel mesh platform to starboard and outside of the operator's cab and a safety screen which, when in the "non-operating" position, lay over the top of the operator's cab and, when in the "operating position," extended over the platform outside the operator's cab. In order to enter the operator's cab, it was necessary to descend four steps, each step consisting of one horizontal steel bar, to reach the steel mesh platform. Once on the steel mesh platform, one would turn left and enter through a door to the operator's cab, which was approximately five feet square. Inside the operator's cab were the controls of the gantry crane and a chair which faced forward, from which the gantry crane operator would operate the gantry crane unit.

7. Libelant had worked on board the SS PRESIDENT TYLER less than seven days and had never worked on a vessel that had a gantry crane prior to signing aboard the SS PRESIDENT TYLER.

8. The gantry crane operator's cab had a safety screen over the top of it, which, if extended to its starboardmost position, engaged an electrical circuit which energized the gantry crane and allowed it to operate. When the safety screen was moved about two to three inches to port from its "operating position," the electrical circuit was de-energized and the gantry crane unit would not operate. Libelant knew how to operate the gantry crane and knew the movement of the safety screen would render the gantry crane inoperative.

9. An injury involving a similar gantry crane had occurred to a seaman aboard a vessel owned and operated by respondent American President Lines prior to the injury occurring to libelant on board the SS PRESIDENT TYLER. This injury occurred before any safety screen was provided. As a result of the previous accident, American President Lines had provided the safety screen to safeguard seamen.

10. The safety screen was of sufficient size to preclude an individual standing on the steel mesh platform from raising his head above the screen vertically, that is, in a direct line perpendicular to the steel mesh platform.

11. A sign was located inside the operator's cab, reading: "Warning. Before moving trolley or boom, clear all men off top of gantry." The "top of the gantry" was not interpreted to include the steel mesh platform.

12. At about 0830 on February 2, 1965, a supervisory employee of Matson Terminals, Inc. complained to libelant that the gantry crane was not operating fast enough and requested libelant to remedy that situation. Pursuant to that request, libelant went to the operator's cab of the gantry crane (which was then occupied by Harry Johnson) and made adjustments which allowed the gantry crane to move athwartship at a faster speed.

13. After libelant made the necessary adjustments to allow the gantry crane to move faster, he stood behind Harry Johnson, inside the cab, and observed the gantry crane operation. Libelant then thought he noticed that an electrical cable leading to the spreader apparatus of the gantry crane had become disengaged from its reel and he told Johnson, the gantry crane operator, that he wanted to inspect the electrical cable and Johnson brought the gantry crane to a stop in response to libelant's request.

14. After waiting for the crane operator, Harry Johnson, to stop the crane, libelant then proceeded to the steel mesh platform outside the operator's cab. At that time the safety screen was at its starboardmost position, which allowed the gantry crane to operate. In order to inspect the electrical cable reel, libelant, by placing his feet on the second rung of the ladder leading to the platform and craning his head outside and atop the safety screen, was able to and did put his head into the space outside the screen, without placing the safety screen in the non-operative position and shutting off the power. Libelant assumed the operator of the gantry crane would not operate the crane while libelant was in a position of

danger. While libelant had his head outside the safety screen, the gantry crane operator started the gantry crane and libelant's head was caught and injured between the outboard portion of the safety screen and a stationary overhead object which came into contact with libelant's head because of the movement of the gantry crane.

15. At all material times the gantry crane was operated by Harry Johnson, an employee of Matson Terminals, Inc.

16. The distance between the safety screen and the steel mesh platform, while the safety screen was extended over the mesh platform, was less than five feet six inches. Libelant was five feet six inches tall.

17. The safety screen was not large enough to prevent partial physical egress from the steel mesh platform and it was physically possible for the safety screen to have been larger.

18. At the time of libelant's accident, the gantry crane, including the safety screen above the steel mesh platform, was in good working order and reasonably fit for its intended use.

19. It was not negligent for libelant to be on the steel mesh platform when the crane was in the operative position, nor was it negligent for the crane operator to operate the crane when libelant was on the steel mesh platform.

20. At the time of his accident, libelant knew that he could have moved the safety screen to the "non-operating position" in a matter of several seconds and knew that he had the right to do so, but did not do so. Libelant fur-

ther knew that, had he done so, the gantry crane unit would have been inoperative. Libelant was negligent in failing to move the safety screen to the "non-operating position" before he placed his head outside the safety screen.

21. It was negligent of the gantry crane operator to operate the gantry crane when libelant was on the platform outside the operator's cab under the circumstances described.

22. The negligence of the gantry crane operator and the negligence of libelant were the sole proximate causes and combined equally to cause libelant's accident and injuries.

23. Respondent provided libelant with a reasonably safe place to work and was not negligent.

24. The vessel and her appurtenances were reasonably fit for their intended use and seaworthy.

25. Libelant has failed to bear the burden of proof that his injuries were caused by any negligence of respondent or unseaworthiness of its vessel or that Matson Terminals, Inc. or its employees were agents of respondent.

26. The damages suffered by libelant, after applying the rule of maritime comparative negligence, would be $7,500, if respondent were legally responsible therefor.

CONCLUSIONS OF LAW

1. This Court has jurisdiction in admiralty under 28 U.S.C. 1333.

2. Respondent does not have the burden of an insurer and is not required to provide an accident-proof vessel and the mere occurrence of an accident does not impose liability upon the vessel owner. The warranty of seaworthiness requires only the furnishing of a vessel and appurtenances reasonably fit for the intended use.

3. There is no cause of action as such for failure to furnish a safe place to work and damages for such failure must be based upon negligence.

4. Libelant has the burden of proving by a preponderance of the evidence that his accident was proximately caused by the negligence of respondent or the unseaworthiness of its vessel.

5. Respondent shipowner was not engaged in a unitary enterprise with an independent stevedore contractor which it did not own or control and whose work in handling cargo it did not control and supervise. Respondent shipowner is not liable, under the doctrine of *Sinkler v. Missouri Pacific Railroad Co.,* 256 U. S. 326 (1958) and *Hopson v. Texaco,* 383 U. S. 262 (1966) for an injury caused by an employee of such an independent stevedore contractor.

6. Respondent was not negligent or otherwise at fault in the premises.

7. Respondent is entitled to a decree dismissing the libel, with costs.

No. 22,395

IN THE

United States Court of Appeals
For the Ninth Circuit

SHAFFER C. TIM,

Appellant,

vs.

AMERICAN PRESIDENT LINES, LTD., a corporation,

Appellee.

Appeal from an Admiralty Decree of the United States District Court for the Northern District of California Honorable Lloyd H. Burke, District Judge

APPELLANT'S CLOSING BRIEF

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

Subject Index

Table of Authorities Cited

Cases

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IN THE

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Appeal from an Admiralty Decree of the United States District Court for the Northern District of California
Honorable Lloyd H. Burke, District Judge

APPELLANT'S CLOSING BRIEF

I

APPELLEE AMERICAN PRESIDENT LINES, LTD., IS LIABLE FOR THE NEGLIGENT ACTS OF THE STEVEDORE'S EMPLOYEE PERFORMED WHILE IN THE COURSE AND SCOPE OF HIS EMPLOYMENT ON BOARD APPELLEE'S VESSEL.

This issue was previously set forth in Appellant's Opening Brief, pages 6 through 13.

Appellee, American President Lines, Ltd., appears to have set forth three responses which it set forth

as though unrelated but would appear to all be covered by appellant's above issue. Appellant will therefore respond to all three issues of Appellee, American President Lines, Ltd., which are set forth in its brief pages 10 through 24.

Appellee, American President Lines, Ltd., is attempting to reraise a long discarded defense. Appellee is attempting to reargue the defense of "fellow servant rule" which has clearly been held inappropriate in an action involving personal injuries to a seaman on board a vessel in navigable waters. (See *Mahnich v. Southern Steamship Company,* 321 U.S. 96, 64 S.Ct. 455.)

It is clear Appellee is attempting to do this in that throughout its arguments it continues to refer to the fact a fellow employee injured plaintiff, that if this was an injury between two longshoremen not on board the vessel that the plaintiff's recourse would be confined to compensation and that previous cases have recognized the difference in years past (but prior to *Mahnich* supra) of the defense of the "fellow servant rule".

It is important to keep in mind that this is an injury to a seaman on board a vessel in navigable waters. This is not an action involving injury to a longshoreman by another longshoreman and is not an injury which occurred shoreside or not on a vessel in navigable waters. However, it is submitted these differentials are not relevant to the case at bar as they also have already been decided by the Supreme Court of the United States as set forth in the authorities below.

In the case of *Mascuilli v. United States,* 387 U.S. 237, 358 F. 2d 133, the United States Supreme Court specifically held that the defendant ship was liable for injuries sustained by a longshoreman (in the case at bar the injuries were sustained by a seaman) when seaworthy equipment was negligently operated by a longshoreman. The court in that decision cited *Mahnich,* 321 U.S. 96, 64 S. Ct. 455 and *Crumady v. Joachim,* 358 U.S. 423, 79 S. Ct. 445.

Two weeks prior to the *Mascuilli* decision the Supreme Court in *Waldron v. Moore-McCormack Lines,* 386 U.S. 724, 87 S. Ct. 1410, arrived at the same conclusion and cited the same two cases (*Mahnich,* supra and *Crumady,* supra).

In the *Waldron,* supra, decision the court stated:

> "In *Mahnich v. Southern Steamship Company,* 321 U. S. 96, the court made it clear that availability of safe and sufficient gear on board does not prevent the actual use of defective gear from constituting unseaworthiness. For the test of unseaworthiness is to be applied 'when and where the work is to be done.'
>
> In *Crumady v. Joachim,* 358 U. S. 423, we further clarified the extent of seaworthiness liability by holding that, even though the equipment furnished for the particular task is itself safe and sufficient, its misuse by the crew renders the vessel unseaworthy. We emphatically stated the basis of our holding:
>
> 'Unseaworthiness extends not only to the vessel but to the crew.'
>
> For that proposition the court cited *Boudoin v. Lykes Brothers,* 348 U. S. 336, 75 S. Ct. 382, where

we said, 'We see no reason to draw a line between the ship and the gear on the one hand and the ship's personnel on the other.'

When this court extended the shipowner's liability for unseaworthiness to longshoremen performing seamen's work, *Seas Shipping Company v. Sieracki,* 328 U. S. 85, 66 S. Ct. 872, either on board or on the pier, *Guitterez v. Waterman Steamship Corporation,* 373 U. S. 206, 83 S. Ct. 1185, either with the ships' gear or the stevedores' gear, *Alaska Steamship Company v. Petterson,* 347 U. S. 396, 74 S. Ct. 601, either as employees of an independent stevedore or as employees of a ship owner *pro hac vice, Reed v. The Yaka,* 373 U.S. 410, 83 S. Ct. 1349, we noted that 'the hazards of marine service, the helplessness of the man to ward off the perils of unseaworthiness, the harshness of forcing them to shoulder their losses alone, and the broad range of the humanitarian policy of the doctrine of unseaworthiness,' id., at 413, 83 S. Ct. at 1352, should prevent the shipowner from delegating, shifting or escaping his duty by using the men or gear of others to perform the ship's work. By the same token the shipowner should not be able to escape liability merely because he has used men rather than machines or physical equipment to perform that work."

In the *Waldron,* supra, decision, there were four dissenting justices who dissented on another ground. However, as to the issue presented to this court the four dissenting justices also recognized that that issue has clearly been resolved by the United States Supreme Court. The dissenting justices said in their first paragraph:

> "Under the prevailing cases in this court there can be no doubt that the negligent or improvident act of a competent officer, crewman, or longshoreman, can result in unseaworthiness if it rendered otherwise seaworthy equipment unfit for the purpose for which it is used. *Crumady v. The Joachim Hendrik Fisser,* 358 U.S. 423, 79 S. Ct. 445."

Since the *Waldron,* supra, decision resolved these issues when the issue was presented again two weeks later in the *Mascuilli,* supra, case the court did not render a written opinion but merely recited the same cases it had cited in the *Waldron,* supra, decision. The *Mascuilli* decision was merely reiterating the long held doctrine that the ship cannot avoid its nondelegable duty, an absolute duty to provide a safe and seaworthy vessel by arguing that it has delegated this duty to a longshoreman as in the case at bar. The Supreme Court held to the contrary and merely reiterated its position that the duty on the part of the shipowner is nondelegable in any manner.

What the Supreme Court has said in the above decisions is that "a seaman's incompetence constitutes unseaworthiness, *Boudoin v. Lykes Brothers,* 348 U. S. 336, 75 S. Ct. 382, the incompetence of a substitute for a seaman would no less constitute unseaworthiness. Similarly since the vessel can become unseaworthy when the stevedoring company puts aboard the defective equipment for use in the ship's work it can also become equally unseaworthy when the stevedore puts aboard defective longshoremen for this same work." (See *Smith v. Lauritzen,* 1962, 201 F. Supp.

663.) That is to say as Justice Douglas pointed out in the *Crumady,* supra, decision:

> "The winch in question was not defective, but the way it was used made it unsafe and dangerous for the work at hand."

The test therefore is, does the condition complained of make the vessel unsafe and dangerous for the work at hand. Or to say it another way as set forth in *Candiano v. Moore-McCormack Lines,* 251 F. Supp. 654 at 656, the practical test is "as it was actually used was the equipment unsafe and therefore unfit."

In no Supreme Court decision is there a holding that the warranty of seaworthiness is anything less than an absolute duty owing to all within the range of its humanitarian policy, one not satisfied by the exercise of due diligence, and inalienable, non-delegable responsibility, a species of liability without fault. The Supreme Court of the United States has enforced this protection with unwavering consistency and has sanctioned no departure from its absolute standard. It is elementary that the crucial consideration is the existence of an unseaworthy condition and not the method of creating said unseaworthy condition if the gear *as actually used*—not as intended to be used but as actually used—or the operation that was *actually performed* was unsafe, the injured longshoreman or seaman is entitled to recovery.

It is to be noted that Appellee, American President Lines, Ltd., at page 23 of its brief relies on the case of *Fenton v. A/S Glittre,* 1967 AMC 317. This decision was affirmed by the Court of Appeals for the Second

Circuit (see 370 F. 2d 146). However, it is this same Court of Appeals for the Second Circuit which subsequent to the *Fenton,* supra, decision stated in *Candiano v. Moore-McCormack Lines,* 382 F. 2d 961, that their previous decisions were incorrect in view of recent Supreme Court decisions. In so concluding the Court of Appeals for the Second Circuit stated in the *Candiano,* supra, decision,

> "The law in this field is now quite clear; any change must be by legislation or by Supreme Court decision."

The preceding discussion deals with the question of seaworthiness. The following discussion deals with the United States Supreme Court's further recognition that a shipping company is not going to avoid its responsibilities in the area of "negligence" on the basis that they have delegated this responsibility to a third party.

In this vein, the United States Supreme Court in *Hopson v. Texaco Incorporated,* 383 U. S. 262, 86 S. Ct. 765, stated:

> "The Jones Act incorporates the standards of the Federal Employers Liability Act as amended which renders an employer liable for the injuries negligently inflicted on its employees, by its officers, agents or employees. We stated in *Sinkler v. Missouri Pacific Railroad Company,* 356 U. S. 326, 78 S. Ct. 758, 2 Lawyer's Ed. 2d 799, that the later act was an avowed departure from the rules of the common law which, recognizing the cost of human injury and an inescapable expense of railroading, undertook to adjust that expense

> equitably between the worker and the carrier. In order to give an accommodating scope . . . to the word 'agents' we concluded that when (an) . . . employee's injury is caused in whole or in part by the fault of others performing under contract, operational activities of his employer, such others are agents of the employer within the meaning of Section 1 of F.E.L.A." (383 U. S. at pages 263-264.)

The court went on to say:

> "This is so because as we said in *Sinkler,* justice demands that one gives his labor to the furtherance of the enterprise should be assured that all combine their exertions with him in the common pursuit will conduct themselves in all respects with sufficient care that his safety while doing his part will not be in danger." (See 383 U. S. page 264.)

Thus on the question of negligence the trial court in the case at bar came to the conclusion that a longshoreman working in the scope and course of his employment was not engaged in the "common endeavor" or that "operational activities" of the vessel. It is submitted that on the question of negligence this conclusion of the trial court is erroneous.

It is to be noted that Appellee, American President Lines, Ltd., attempts to distinguish the *Hopson* decision relative to the argument of negligence on the grounds that it, American President Lines, did not have a direct contractual relationship with the stevedoring company.

This argument is superfluous for the following reasons: (1) The trial court in its findings concluded, "There contracts were not regarded by the trial judge as having any significance insofar as the judgment reached was concerned." (See finding of fact number three.) (2) An Appellate Court of the United States has recognized that the stevedoring contracts with shipping companies give rise to third party contractual rights to injured employees on board a vessel in navigable waters. (*Sanderlin v. Old Dominion Stevedoring,* 385 F. 2d 79.) (3) The very essence of the *Hopson,* supra, decision was based on the premise that a shipowner had a nondelegable duty and should not be able to escape liability merely because the shipowner has used men rather than machines or physical equipment to perform the work it is obligated to perform.

It is submitted the facts presented to this court clearly substantiate the proposition that Appellee, American President Lines, is liable for the injuries sustained by the Appellant both on the grounds of the doctrine of unseaworthiness (*Waldron,* supra, *Mascuilli,* supra, *Candiano,* supra), and based on the doctrine of negligence (*Hopson,* supra, and *Sinkler,* supra).

II

THE PLAINTIFF, A SEAMAN IN THE EMPLOY OF DEFENDANT, WHILE ACTING IN THE COURSE AND SCOPE OF HIS EMPLOYMENT, HAS A RIGHT TO RELY ON THE STEVEDORE PERFORMING HIS DUTY WITH CARE AND IS, THEREFORE, NOT CONTRIBUTORILY NEGLIGENT.

The United States Supreme Court in *Hopson v. Texaco, Inc.,* 383 U. S. 262, 86 S. Ct. 765, stated:

> "This is so because as we said in *Sinkler* justice demands that one who gives his labor to the furtherance of the enterprise should be assured that all combining their exertions with him in the common pursuit will conduct themselves in all respects with sufficient care that his safety while doing his work will not be in danger." (See 383 U.S. at page 264.)

Appellant, Shaffer C. Tim, in his opening brief, pages 13 through 19 sets forth authorities which substantiate the proposition that appellant was under no duty to exercise care to discover extraordinary dangers that may arise in the negligence of the shipowner or those for whose conduct the shipowner is responsible, but that the plaintiff may assume that the employer or his agent have exercised proper care for his safety until notified to the contrary.

The trial court found that "libelant assumed the operator of the gantry crane would not operate the crane while libelant was in a position of danger." (See Finding of Fact Number 14, lines 26 to 27.) And further found that "it was negligent of the gantry crane operator to operate the gantry crane while libelant was on the platform outside the operator's cab

under the circumstances described." (See Finding of Fact Number 21.)

Appellant in his opening brief sets forth the authorities that stand for the proposition that the appellant had the right to presume that the negligent employee of the defendant involved would do his duty and that under such circumstances the plaintiff could not be considered to have also been negligent for presuming that defendant's employee would do his duty.

It is reiterated that it is incongruous to hold that by exercising a right plaintiff can in any degree be negligent. The trial court concluded that plaintiff would not have placed himself in the position he did had he known the crane was going to operate and that plaintiff, in fact, never expected the crane operator to "be stupid enough to start the equipment." (See Court's expression in Reporter's Transcript, page 33, lines 16-22.)

III

THE TRIAL JUDGE AS A TRIER OF FACT CANNOT MAKE A FINDING ON DAMAGES AFTER HAVING ONCE FIRST CONCLUDED THERE IS NO LIABILITY ON THE PART OF DEFENDANT.

Appellant has set forth his arguments substantiating the above proposition in his opening brief, pages 19 through 24.

The appellee cites the case of *United States v. Woodbury,* 359 F. 2d 370, 379, as authority for its position.

It is submitted this case does not stand for appellee's proposition in that the question of damages in that case turned on a question of law. That is to say, if the trial court in the *Woodbury,* supra, decision was correct on its factual findings then as a matter of law the amount of damages was appropriate. This is not the situation as presented to this court.

In the *Woodbury* decision with regard to the question of damages on appeal the appellate court found, in that particular action that the trial court was correct in finding that no damages were recoverable. In that case there were four appeals and two motions before the court. On one of the appeals, the trial court had concluded that no damages were recoverable by the United States. The appellate court affirmed that decision.

In the case at bar, appellant contends that the trial court was in error as to the amount of damages it purportedly awarded because appellant in fact was not contributorily negligent. If in fact appellant is correct in this position, then it is submitted the trial court cannot bind the appellate court as to the amount of damages that should be awarded in the event the appellate court concludes that appellant is correct and that he was not in fact contributorily negligent.

In addition, even if this court should find that the trial court was correct on its conclusion of law with regard to whether appellant can be contributorily negligent when exercising a right recognized by law, then appellant further contends this court is deprived of its recognized appellate right to review the trial

court's findings of fact with which it substantiated its conclusions as to the amount of damages. Therefore the trial court is further in error in that it deprives this appellate court of its procedural rights to review the trial court's findings of facts in order to determine whether the trial court's conclusions as to the amount of damages were sustained by the evidence.

Dated, San Francisco, California,
May 31, 1968.

JARVIS, MILLER & STENDER,
By R. JAY ENGEL,
Attorneys for Appellant.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

R. JAY ENGEL,
Attorney for Appellant.

/ /

Nos. 22,397 and 22,398

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant

v.

CALIFORNIA PORTLAND CEMENT CO.,

Appellee

ON APPEALS FROM THE JUDGMENTS OF THE UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

BRIEF FOR THE APPELLANT

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I N D E X

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

Nos. 22,397 and 22,398

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Appellant

v.

CALIFORNIA PORTLAND CEMENT CO.,

Appellee

ON APPEALS FROM THE JUDGMENTS OF THE UNITED STATES
DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

BRIEF FOR THE APPELLANT

OPINION BELOW

The findings of fact and conclusions of law of the District Court (No. 22,397, I-R. 119-130; No. 22,398, I-R. 176-191) are not officially reported.

JURISDICTION

These appeals involve federal corporate income taxes and excess profits taxes paid by the taxpayer for its taxable years ended April 30, 1953, April 30, 1954, April 30, 1955, April 30, 1956, April 30, 1957, April 30, 1958, and April 30, 1959 (No. 22,398, I-R. 177), and federal corporate income taxes and excess profits

taxes paid by taxpayer's predecessor in interest, Arizona Portland Cement Company, for its taxable years ended April 30, 1953, April 30, 1954, April 30, 1955, April 30, 1956, and April 30, 1957 (No. 22,397, I-R. 120-121). Arizona Portland Cement Company was merged into taxpayer on August 31, 1961, and taxpayer thereby succeeded to the rights of Arizona Portland Cement Company under its pending claims for refund. (No. 22,397, I-R. 120.) The taxes in dispute were timely paid and claims for refund were timely filed.[1/] Within the time provided by Section 3772 of the Internal Revenue Code of 1939 and Section 6532 of the Internal Revenue Code of 1954, on June 2, 1965, the taxpayer brought these actions in the District Court for recovery of the taxes paid by itself and by its predecessor in interest, Arizona Portland Cement Company. (No. 22,397, I.R. 2; No. 22,398, I-R. 2.) Jurisdiction was conferred on the

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1/ This jurisdictional statement would be extended to an inordinate length by a particularization of the dates and amounts of the payments and the dates on which the various claims for refund were filed and successively amended. For the dates and amounts of the payments by taxpayer which the District Court has ordered refunded, see No. 22,398, I-R. 190-191. For the dates and amounts of the payments of Arizona Portland which the District Court has ordered refunded to taxpayer as Arizona Portland's successor in interest, see No. 22,397, I-R. 129-130. The dates on which taxpayer's claims for refund were filed and successively amended, the timeliness of such filings and amendments, and the timeliness of the suit for refund, the claims having neither been allowed nor disallowed, have all been stipulated. (No. 22,398, I-R. 135, 145-146, 148-149, 151-152, 154-162.) These matters are likewise stipulated as to Arizona Portland's claims for refund and the suit thereon. (No. 22,397, I-R. 90, 97-99, 101-105, 107-110.)

District Court by 28 U.S.C., Section 1346. The judgments of the District Court were entered on March 23, 1967. (No. 22,397, I-R. 147; No. 22,398, I-R. 225.) On April 3, 1967, the Government filed motions for amendment of the findings and judgments and for a rehearing. (No. 22,397, I-R. 151; No. 22,398, I-R. 226.) These motions were denied on July 31, 1967. (No. 22,397, I-R. 162; No. 22,398, I-R. 237.) Within sixty days thereafter, on September 28, 1967, the Government filed its notices on appeal. (No. 22,397, I-R. 163; No. 22,398, I-R. 238.) Jurisdiction is conferred on this Court by 28 U.S.C., Section 1291.

QUESTIONS PRESENTED

Under the cost-oriented proportionate profits method, concededly applicable here, the depletable mining income of an integrated miner-manufacturer is the portion of its total gross income from the manufactured product which is produced by mining costs, and this portion is determined by the ratio of mining costs to the total costs (mining and non-mining) which produced the total gross income.

The questions presented are whether the District Court has erroneously interpreted and applied the proportionate profits method in the following respects:

1. In allocating to mining costs the expenses of handling

and storing purchased mineral materials (additives) prior to their addition to the kiln feed.

2. In excluding from the computation the income from sales of bagged cement, the costs producing such sales and certain selling expenses.

3. In failing to include the costs of bags and bagging and the selling expenses as non-mining costs in their entirety.

4. In allocating between mining and non-mining income an inflated gross income figure based on list prices rather than on the actual receipts produced by the so-called discount prices.

STATUTES AND OTHER AUTHORITIES INVOLVED

The statutes and other authorities involved are set forth in Appendix A, infra.

STATEMENT

The material facts, as found by the District Court (No. 22,397, I-R. 120-127; No. 22,398, I-R. 176-187), may be summarized as follows:

During the taxable years involved, taxpayer was a California corporation with its principal offices in Los Angeles, and Arizona Portland Cement Company (hereinafter "Arizona Portland") was an Arizona corporation with its principal offices in Tucson, Arizona. Both corporations kept their books and filed their returns on the basis of a taxable year ended April 30 and the accrual method

of accounting. Arizona Portland was merged into taxpayer on August 31, 1961, and taxpayer thereby succeeded to the rights of Arizona Portland under its pending claims for refund for its fiscal years ended April 30, 1953-April 30, 1957. (No. 22,397, I-R. 120-121; No. 22,398, I-R. 176-177.)

The principal business of both corporations during the taxable years was the manufacture and sale of finished cement (Portland and allied types). Taxpayer conducted this business in its plant at Colton, California, and (commencing in the taxable year ended April 30, 1956) in its plant at Mojave, California. Taxpayer owned a deposit of calcium carbonate rock (limestone) immediately adjacent to its Colton plant and another immediately adjacent to its Mojave plant. Arizona Portland manufactured cement in its plant at Rillito, Arizona, immediately adjacent to which the corporation owned a deposit of calcium carbonate rock (limestone). Taxpayer and Arizona Portland extracted the calcium carbonate rock from the said deposits and produced cement clinker and finished cement from such rock in the adjacent plants by the application of the ordinary treatment processes normally applied by mine owners and operators in the cement industry having similar deposits. (No. 22,397, I-R. 121; No. 22,398, I-R. 177-178.)

At no time during the taxable years was there any commercial market for the calcium carbonate rock extracted and used by the

corporations in manufacturing cement, within the market areas respectively available to taxpayer and Arizona Portland, at any stage of extraction or processing (apart from minor sales of cement clinker) prior to the production of finished cement. The corporations supplied only a portion of the demand for finished cement in the market areas respectively available to them. (No. 22,397, I-R. 122-123; No. 22,398, I-R. 182.) Taxpayer sold an average of 4.9 per cent of its cement clinker, during the taxable years, to Blue Diamond Corporation. Arizona Portland sold approximately 2.6 per cent of its cement clinker, during the taxable year ended April 30, 1957, to Southwestern Portland Cement Company. Blue Diamond and Southwestern Portland were the only concerns, within the market areas respectively available to taxpayer and Arizona Portland, which purchased cement clinker for production of finished cement. There was no commercial market, within the said market areas, for any additional amounts of clinker or for any mineral product of like kind and grade at any earlier stage of extraction and processing. The clinker sold by the corporations could not have been produced and sold on a commercial basis except as by-products incident to the corporations' cement-producing operations, and the sales did not establish any representative market or field price for the calcium carbonate rock used by the corporations in producing cement. (No. 22,397, I-R. 121-122; No. 22,398, I-R. 180-181.)

In its Colton plant taxpayer used limited amounts of calcium carbonate rock extracted from its adjacent deposit to produce ground rock for sale as glass sand, poultry grits, roofing grits and miscellaneous purposes; to produce finished lime products (lump lime, ground quicklime and hydrated lime); and to produce paving dust (fines). The calcium carbonate rock so used was not of like kind and grade to the calcium carbonate rock used by taxpayer in its principal business, producing and selling cement. The ground rock, lime products and paving dust could not have been produced and sold by taxpayer on a commercial basis except as by-products incident to taxpayer's cement-producing operation, and the sales of such by-products did not establish any representative market or field price for the calcium carbonate rock used by taxpayer in producing cement. (No. 22,398, I-R. 178-181.)

The calcium carbonate rock extracted by the corporations from their deposits had an average total carbonates content of approximately 80 per cent, and were not "marble" but "limestone" or "calcium carbonates" within the commonly understood meaning of those terms. It was not economically or commercially feasible for taxpayer or Arizona Portland to use any of their calcium carbonate rock in the production of dimension stone. (No. 22,397, I-R. 122; No. 22,398, I-R. 181.)

In their cement-producing operations, taxpayer and Arizona Portland added iron ore and quartzite to their calcium carbonate

rock in the raw grinding stage prior to the introduction of the raw mix into the kiln. The addition of these mineral materials was an essential step in the production of their cement clinker and finished cement. Subsequent to the corporations' acquisition of the iron ore and quartzite, but prior to their admixture with the calcium carbonate rock, these mineral materials were stored on the corporations' premises and then moved to the point of admixture. (No. 22,397, I-R. 123; No. 22,398, I-R. 182-183.)

In the context of the foregoing primary findings, the District Court entered a conclusory finding that the corporations' costs of storing and handling the purchased mineral materials, prior to their admixture with the calcium carbonate rock, should be treated as mining costs. (No. 22,397, I-R. 123; No. 22,398, I-R. 183.) The Government contends that this finding is erroneous as a matter of law.

Taxpayer and Arizona Portland offered to their customers, after sale, a discount of 20 cents per barrel of finished cement. Taxpayer offered a similar discount with respect to its paving dust and ground calcium carbonate rock. (No. 22,387, I-R. 123; No. 22,398, I-R. 182.)

With respect to these discounts, the District Court entered a finding that they were offered for the purpose of inducing prompt payment and not for the purpose of inducing sales, and were cash

discounts rather than trade discounts. (No. 22,397, I-R. 123; No. 22,398, I-R. 182.) The Government contends that this finding is unwarranted by the record and erroneous.

In November, 1960, timely elections were filed by taxpayer and Arizona Portland to have the provisions of Section 302(b) of the Public Debt and Tax Rate Extension Act of 1960, Appendix, infra, apply to the computation of their percentage depletion allowances for all open taxable periods, which included the taxable years involved in this litigation. Their depletion allowances for the taxable years with respect to their calcium carbonate rock used in the production of cement clinker and finished cement are to be computed under the proportionate profits method prescribed in Treasury Regulations 118, Section 39.23(m)(e)(3), Appendix, infra, by reference to a cutoff at the kiln-feed point after mixing and grinding. (No. 22,397, I-R. 124; No. 22,398, I-R. 183-184.)

The District Court entered a conclusory finding that the "first commercially marketable product" of the corporations' cement-producing operations was bulk cement, and that both the additional income and the additional costs attributable to sales in sacks should be excluded from the computation of the corporations' depletion allowances. (No. 22,397, I-R. 124-125; No. 22,398, I-R. 184-185.) The Government contends that this finding is erroneous as a matter of law.

During the taxable years, taxpayer and Arizona Portland incurred certain selling expenses with respect to their products, consisting primarily of salaries and other expenses of salesmen, and membership in various industry trade associations. (No. 22,397, I-R. 125; No. 22,398, I-R. 185.)

The District Court entered a conclusory finding that because, in its view, the said selling expenses did not "represent the cost of any process" applied to the corporations' calcium carbonate rock, they should be excluded from the computation of the corporations' depletion allowances. Alternatively, the court found that, if the computation under the proportionate profits method prescribed in Regulations should include costs other than "direct process costs", the selling expenses should be allocated "to both the mineral product and the manufactured product because such expenses were necessary to and of benefit to both such products". (No. 22,397, I-R. 125; No. 22,398, I-R. 185.) The Government contends that these findings are erroneous as a matter of law.

The District Court entered conclusions of law in accordance with its findings (No. 22,397, I-R. 127-130; No. 22,398, I-R. 188-191), and judgments in favor of taxpayer in the amounts of $93,618.38 and $240,244.99, with statutory interest (No. 22,397, I-R. 147; No. 22,398, I-R. 225).

SPECIFICATION OF ERRORS RELIED UPON

The Government contends that the District Court erred in the following respects:

1. (a) In ruling that the costs of storing and handling purchased or fully depleted mineral materials, prior to their addition to the kiln feed, were costs of mining processes as defined by the applicable statutory provisions; and (b) in allocating such expenses, in the proportionate profits computation, to mining costs.

2. (a) In ruling that the "first commercially marketable product" was bulk cement only, notwithstanding the fact that the finished cement was sold both in bulk and in bags; (b) in excluding the income from sales of bagged cement, and the costs producing such sales, from the proportionate profits computation; and (c) in failing to include such costs in the computation as non-mining costs in their entirety.

3. (a) In ruling that certain expenses of selling the finished cement (primarily the salaries and other expenses of salesmen and membership in trade associations) should be excluded from the proportionate profits computation; and (b) in failing to include such expenses in the computation as non-mining costs in their entirety.

4. (a) In ruling that discounts to customers were offered exclusively for the purpose of inducing prompt payment, and not for the purpose of inducing sales, although the so-called discount

prices were set in competition with other members of the cement industry and produced the corporations' actual receipts; and (b) in allocating between mining and non-mining income, in the proportionate profits computation, an inflated gross income figure based on the corporations' list prices rather than on the actual receipts produced by the so-called discount prices.

SUMMARY OF ARGUMENT

The taxpayer is an integrated miner-manufacturer of cement, as was its predecessor in interest, Arizona Portland. An integrated cement producer mines the principal ingredient of cement, calcium carbonate rock, and grinds it together with other mineral materials (additives) into a raw mix known as kiln feed. Under the applicable statutory provision, the preparation of the kiln feed terminates the mining phase of the producer's operations. Thereafter, the producer manufactures cement from the kiln feed and sells the finished cement in bulk and bags. All of the producer's costs in mining, manufacturing and marketing the cement were reflected in the prices charged customers.

The depletable mining income of an integrated producer of cement is its constructive income from the raw mineral product of mining (kiln feed) which he is deemed to sell to himself. Long-established Tressury Regulations prescribe the proportionate profits method of computing an integrated producer's constructive

mining income where, as here, there is no representative price in the industry for the product of mining. Under the proportionate profits method, the producer's gross income from sales of its manufactured product is allocated between mining and non-mining income in the ratio that mining costs bear to the total costs of producing the sales. Every dollar of income and every dollar of costs must go into the computation. To the extent that non-mining costs are treated as mining costs, or omitted from the computation, the net effect is to give the producer depletion on non-mining income.

In the instant case, the District Court erroneously allocated non-mining costs to mining costs (i.e., the expenses of handling and storing minerals other than calcium carbonate rock), and erroneously omitted from the computation altogether non-mining costs underlying the sales of finished cement (i.e., the costs of bags and bagging, and certain selling expenses). The court also erroneously distorted the gross income from sales of cement by omitting income from sales of bagged cement, and by treating list prices as the selling prices, whereas the co-called discount prices were the actual selling prices and were reflected in the actual gross sales.

ARGUMENT

I

THE DISTRICT COURT HAS ERRONEOUSLY INTERPRETED AND APPLIED THE PROPORTIONATE PROFITS METHOD AND THEREBY HAS ALLOWED DEPLETION ON NON-MINING INCOME

A. The proportionate profits method and its statutory context in this litigation

Section 611(a) of the Internal Revenue Code of 1954, Appendix A, *infra*, provides in pertinent part that in "the case of mines, * * * [and] other natural deposits, * * * there shall be allowed as a deduction in computing taxable income a reasonable allowance for depletion * * *, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under regulations prescribed by the Secretary or his delegate". 2/ Section 613(a), Appendix A, *infra*, provides that "the allowance for depletion under section 611 shall be the percentage, specified in subsection (b), of the gross income from the property * * *." Section 613(c)(1), Appendix A, *infra*, defines "gross income from the property" in the case of a property other than an oil or gas well, as "gross income from mining", and Section 613(c)(2), Appendix A, *infra*, defines "mining".

2/ For the taxable years ended April 30, 1953, and April 30, 1954, the depletion allowance was authorized by Section 23(m) of the Internal Revenue Code of 1939. The provisions governing percentage depletion and defining "gross income from mining", now contained in Section 613 of the 1954 Code, were contained in Section 114 of the 1939 Code. Apart from changes in percentage rates, the relevant provisions in the two Codes are substantially similar, save as noted in the text. In the main, therefore, only the 1954 Code provisions will be cited and quoted, in the interest of simplicity.

As originally enacted, Section 613(c)(2) carried over the definition of "mining" in Section 114(b)(4)(B) of the 1939 Code, as including --

> not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals * * * from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills.

In short, depletable income from "mining" was income from the "commercially marketable" product of "ordinary treatment processes normally applied by mine owners or operators * * *."

Section 613(c)(4), as originally enacted, set forth examples of "ordinary treatment processes" which were part of "mining". As to many minerals, however, including calcium carbonates, fire clay and shale, the statute provided no definite guidelines as to what constituted "ordinary treatment processes" and a "commercially marketable" product. Controversies over these terms were complicated in the case of integrated miner-manufacturers whose gross income was only from sales of their finished manufactured products.

Basic principles for determining the depletable "gross income from mining" of an integrated miner-manufacturer were finally supplied by the Supreme Court in United States v. Cannelton Sewer Pipe Co., 364 U.S. 76. There the taxpayer mined fire clay and shale and manufactured them into sewer pipe and other vitrified products. It claimed the depletion allowance on its gross sales of the manufactured products, contending that these products were the first "commercially marketable" result of "ordinary treatment processes" because it could not sell its raw minerals at a profit. Rejecting this contention, the Supreme Court held that (p. 86) "Congress intended to grant miners a depletion allowance based on the constuctive income from the raw mineral product if marketable in that form", and that raw minerals are "commercially marketable" under the statute when "ready for industrial use or consumption" -- whether or not a taxpayer can sell them at a profit.[3/]

3/ In Cannelton the Court noted that there were non-integrated miners of fire clay who sold the raw mineral product. However, it is settled that the Cannelton principles apply even to a completely integrated industry where there are no sales of the raw mineral. Riddell v. Monolith Cement Co., 371 U.S. 537; United States v. Longhorn Portland Cement Co., 328 F. 2d 491 (C.A. 5th); United States v. Light Aggregates, Inc., 343 F. 2d 429 (C.A. 8th).

The Court further held that (p. 89) "Congress intended integrated mining-manufacturing operations to be treated as if the operator were selling the mineral to himself for fabrication", and, more specifically, that an integrated taxpayer's constructive "gross income from mining" should be computed at the processing point where a non-integrated miner would be ready to ship and sell the minerals. Generally, the Court emphasized (p. 88) that depletion is an allowance "for exhaustion of minerals alone", and cannot be extended for the benefit of a miner-manufacturer to "a similar allowance on his manufacturing costs, including depreciation on his manufacturing plant, machinery and facilities."

Thereafter, Congress undertook to spell out more specifically what constituted mining processes and where they ended (the so-called mining cutoff point). Section 613 was amended in 1960 by Section 302(b) of the Public Debt and Tax Rate Extension Act of 1960, Appendix A, <u>infra</u>, to define "mining" in subsection (c)(2) as including not merely extraction but "also the treatment processes considered as mining described in paragraph (4) (and the treatment processes necessary or incidental thereto)" plus transportation defined as before. Section 613(c)(4), which had theretofore set forth examples of "ordinary treatment processes", was amended to provide in pertinent part:

> The following treatment processes where applied by the mine owner or operator shall be considered as mining to the extent they are

> applied to the ore or mineral in respect of which he is entitled to a deduction for depletion under section 611.
>
> * * * * *
>
> (F) in the case of calcium carbonates and other minerals when used in making cement--all processes (other than preheating of the kiln feed) applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process; * * *

The new definitions of mining processes were originally applicable only to taxable years beginning after December 31, 1960. (Section 302(c), Appendix A, infra.) Thereafter, however, by Section 4 of the Act of September 14, 1960, Appendix A, infra, the new definitions were made retroactive to earlier years at the election of taxpayers. In the instant case, taxpayer and Arizona Portland timely elected to compute their "gross income from mining" for all of the taxable years involved under the new Section 613(c)(4)(F). Hence their "mining' of minerals "in respect of which" they were entitled to depletion ended with the final preparation of the kiln feed.

The specific methods by which "gross income from mining" shall be computed are set forth in the long-standing provisions of Section 39.23(m)-1(e)(3) of Treasury Regulations 118 (1939 Code), Appendix A, infra, which are applicable to all taxable years beginning after December 31, 1951. 4/ These provisions deal first with the simple

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4/ Although Treasury Regulations 118 were promulgated under the 1939 Code, they are applicable under the 1954 Code until superseded by new Regulations. Section 7807 of the 1954 Code, Appendix A, infra. New Regulations have been proposed but have not yet been promulgated.

situation where a miner sells his crude mineral in the immediate vicinity of the mine, without processing it beyond the mining cutoff point. In that situation, the miner's "gross income from mining" is equivalent to its gross sales. If, however, the taxpayer applied non-mining processes before sale, or transports the crude mineral before sale beyond the immediate vicinity of the mine, then its "gross income from mining" is not its gross sales but --

> the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes actually applied, before transportation of such product (other than by transportation treated, for the taxable year, as mining). 5/

Finally, Section 39.23(m)-1(e)(3) deals with situations where there is no representative market or field price for the product of mining, i.e., where there is a largely integrated industry in which the crude mineral is generally not traded and sold because almost every member of the industry mines his own minerals and uses them in manufacturing the end product. That is concededly the situation here with respect to the kiln feed. Under such

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5/ Section 39.23(m)-1(e)(3) equates mining processes with "ordinary treatment processes", in accordance with the statutory definition of mining in force when Treasury Regulations 118 were adopted. Now, of course, the provision must be read in terms of the treatment processes defined as mining in Section 613(c)(4).

circumstances, the regulation provides that the constructive "gross income from mining" of the miner-manufacturer shall be computed as follows:

> If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes * * * minus the costs and proportionate profits attributable to the transportation (other than transportation treated, for the taxable year, as mining) and the processes beyond the ordinary treatment processes. * * *

This prescription (hereinafter "the proportionate profits method") is followed by the proviso that a method of computation other than a "computation of profits proportionate to costs" may be used if the taxpayer establishes to the satisfaction of the Commissioner that the proposed method clearly reflects the taxpayer's gross income from mining.

In United States v. Portland Cement Co. of Utah, 378 F. 2d 91 (C.A. 10th), the court said of the regulation and the proportionate profits method (p. 94):

> The decision in Douglas v. Commissioner of Internal Revenue, 322 U.S. 275, 281, points out that because Congress "obviously could not foresee the multifarious circumstances which would involve questions of depletion, it delegated to the Commissioner the duty of making the regulations." Here we are concerned with a regulation of more than 25 years standing. It has been before the courts a number of times without question

> of its underlying validity being raised. The taxpayer has the burden of showing both that the proportionate-profits method of the regulations is unreasonable and that its substitute-materials method is reasonable.

In the instant case, the District Court found that the proportionate profits method as prescribed by the regulation was applicable (No. 22,397, I-R. 124; No. 22,398, I-R. 184), and taxpayer did not disagree. Indeed, in its returns for the taxable years, taxpayer purported to use the proportionate profits method in computing its "gross income from mining", and since then has never claimed that it is entitled to use another method. (No. 22,397 and No. 22,398 Pltf. Ex. 20 A-D, pp. 325-326, 332-333.)[6/] However, as will appear, the rulings of the District Court are irreconcilable with the proportionate profits method and have allowed depletion on income which is clearly non-mining in character.

Before turning to the specific issues, it is important to consider with care the exact nature of the proportionate profits method and the basic principles which must govern its application.

In Whitehall Cement Manufacturing Co. v. United States, 369 F. 2d 468, 472 (C.A. 3d), the court aptly described the method as "cost oriented" and as requiring "an allocation of [the taxpayer's] total gross income between mining and non-mining operations in the

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6/ Plaintiffs' Exhibit 20 A-D is a four-volume compilation of depositions.

proportion which mining costs bear to the total costs of the cement sold". As set forth in Whitehall, the required allocation of gross income is reflected in the following mathematical formula:

$$\frac{\text{Mining costs}}{\text{Total (mining plus non-mining costs)}} \times \text{gross sales} = \text{gross income from mining}$$

The application of this formula does not turn upon accounting concepts; it is controlled by the tax concept of "gross income from mining", which, in the case of an integrated miner-manufacturer, means his constructive income from the raw mineral product of "mining". United States v. Portland Cement Co. of Utah, supra; United States v. Cannelton Sewer Pipe Co., supra.

As indicated in the Whitehall statement of the formula, the total income which is to be allocated between mining and non-mining is, as a practical matter, the taxpayer's total gross income from sales of its manufactured product. The regulation defines the amount to be allocated as "the representative market or field price of the first marketable product" -- which is the sales price actually charged and collected by the taxpayer, absent a showing to the contrary, for its manufactured end product (here, finished cement).

Two basic principles govern the allocation of gross sales between mining and non-mining income:

1. Every dollar of the costs that have produced the gross sales must go into the computation; and

2. Every dollar of such costs is treated as earning the same percentage of profits.

As the Court of Claims said in Standard Lime and Cement Co. v. United States, 329 F. 2d 939, 944, the method is centered on the "basic assumption * * * that each dollar of costs expended to produce and sell the end product earns the same percentage of the profit". (Emphasis supplied.) Accord, United States v. Portland Cement Co. of Utah, supra. This approach is the very heart of the cost-oriented proportionate profits method, and any departure produces a distorted result.

Thus, elimination of any item of cost from the computation distorts the allocation of the taxpayer's gross sales. Equally, the allocation is distorted if any costs other than those properly attributable to mining, as defined in the statute, are allocated to the numerator of the cost fraction (mining costs). Every dollar of the costs expended to produce and sell the manufactured product, other than mining costs, must be allocated to the denominator of the fraction (total, or mining plus non-mining costs). If costs other than those of mining are allocated to the numerator, or omitted from the denominator, the resulting allocation extends the depletion allowance to non-mining income, contrary to the statute.

The degree of difficulty in identifying costs as mining or non-mining varies with the type of cost. The costs of extraction

and the processes defined in the statute as mining are (to the extent the processes are applied to the minerals mined by the taxpayer) clearly mining costs. The costs of manufacturing processes are, of course, non-mining. As for other costs of producing and selling the manufactured end product, the Court of Claims held in Standard Lime and Cement Co., supra, that such costs are allocable to mining only to the extent that they are incurred for the benefit of the mining phase of the integrated producer's operations. The court emphasized that the Congressional intent underlying the depletion provisions requires a clear showing of benefit to mining and to the raw mineral product of mining (kiln feed, there as here). It said in part (329 F. 2d, p. 946):

> We believe that Congress intended to include in gross income from mining only those cost items (and a percentage of the entire profit attributable to them) which were incurred for the benefit of the mining operations as defined in section 613(c)(4). This result is inescapable since we must view depletion as "an allowance for the exhaustion of a capital asset." United States v. Cannelton Sewer Pipe Co., supra, at 86, * * * This capital asset under the statutory definition is measured for depletion purposes in terms of "gross income from mining." It follows that only those costs incurred for the benefit of the mining operation as particularized by the statutory scheme, can be included. The language of subparagraph (F) of subsection 613(c)(4) demands this conclusion, for it specifically includes all processes up to kiln feed "but not including any subsequent processes." [Emphasis in original.] We interpret this as excluding any subsequent manufacturing

> or marketing processes. Admittedly, our holding might be contrary to accepted cost accounting principles, but the purpose of depletion allowance is not to recompense for the cost of manufacturing and marketing of the end product but is to allow for the exhaustion of the mineral assets. Thus the depletion rate must be applied as nearly as possible to the income derived from the mining of the raw materials as defined in the statutory scheme. [Emphasis supplied.]

We submit that the Court of Claims' approach is sound, and hence that no part of an integrated producer's costs (other than direct mining process costs) may be allocated to mining unless there is a discernible, demonstrable benefit to mining and the crude mineral product thereof. As will appear, the Third Circuit has taken the same approach in Whitehall in deciding issues which included some of the very questions presented here.

II

THE DISTRICT COURT ERRED IN ALLOCATING TO MINING COSTS THE EXPENSES OF SEPARATELY HANDLING AND STORING MINERAL MATERIALS (ADDITIVES) OTHER THAN CALCIUM CARBONATE ROCK

While calcium carbonate rock is the principal ingredient of cement, it was necessary for taxpayer and Arizona Portland to add certain mineral materials in the raw grinding stage to produce the proper blend in the kiln feed. These additives (iron ore and quartzite) were stored separately prior to the raw grinding stage. The corporations purchased the additives save in the case of the

iron ore used by taxpayer, which taxpayer mined from its own deposits. The question is whether the costs of separately storing and handling the additives, prior to raw grinding, were allocable to mining costs in the proportionate profits computation. It is stipulated that these costs (kept separately on taxpayer's books) do not include the costs of the physical addition of the additives to the calcium carbonate rock. (Pltf. Ex. 20 A-D, p. 214.) Hence the costs of physical addition are not involved here.

The District Court ruled that the costs of handling and storing the additives were costs of mining "treatment processes" applied by the corporations to their calcium carbonate rock, under the statute. (No. 22,397, I-R. 128; No. 22,398, I-R. 189.) Hence it ruled that such costs were allocable to mining costs in the proportionate profits computation. (No. 22,397, I-R. 123; No. 22,398, I-R. 182-183.) We submit that these rulings were erroneous.

Section 613(c)(4), in the amended form applicable to the taxable years involved, provides in its preamble that the "treatment processes" enumerated therein "shall be considered as mining to the extent they are applied [by the mine owner or operator] to the ore or mineral in respect of which he is entitled to a deduction for depletion under section 611 * * *". This litigation involves the computation of depletable mining income from calcium carbonate rock used in the production of finished cement. Hence only "treatment

processes" applied to calcium carbonate rock are "mining" processes within the purview of the statute. It should be obvious that the separate handling and storage of mineral materials other than calcium carbonate rock are not "treatment processes" applied to the ore or mineral "in respect of which" the taxpayer and Arizona Portland are entitled to a deduction for depletion.

This Court has already dealt with the governing criteria in Riddell v. California Portland Cement Co., 330 F. 2d 16. There the instant taxpayer contended that its costs of purchasing the quartzite and mining the iron ore were costs of "treatment processes * * * considered as mining" with respect to its calcium carbonate rock. This Court rejected the contention. As for the iron ore mined by taxpayer, the Court noted that taxpayer had already been allowed depletion on such ore; that separate depletion of the mineral components of the kiln feed was required by law; and that allowing the taxpayer to include the costs of mining the iron ore in its costs of mining calcium carbonate rock would give the taxpayer double depletion on the iron ore. As for the quartzite, the Court said (p. 18):

> If inclusion of iron ore extracted by taxpayer is improper, *a fortiori* inclusion of quartzite purchased from someone else is improper. Taxpayer has no "economic interest" in the quartzite.

The Court quoted from the legislative history of the 1960 amendments to Section 613(c)(2)(4), i.e, H. Conference Rep. No. 2005,

86th Cong., 2d Sess., pp. 8-9 (1960-2 Cum. Bull. 741, 746), Appendix A, <u>infra</u>, this significant passage:

> As under existing law, a described process is to be treated as mining where performed by another person for the mineowner or operator if the mineowner or operator has not disposed of his depletable interest in the ore or mineral to which such process is applied. Under the language of this provision, a described process is not treated as mining where applied to a purchased ore or mineral.

Emphasizing the limitation in the preamble to Section 613(c)(4), the Court concluded (pp. 18-19):

> The depletion allowance sought here is in respect of limestone. Under the <u>Cannelton</u> doctrine, "mining" ceases at the crushing stage. * * * The Congress granted relief from this rule by including treatment processes applied to the mineral up to the kiln-feed stage. Surely Congress did not mean to grant the additional relief of allowing depletion upon minerals already depleted or in which the taxpayer had but an "economic advantage."

Without more, we submit that the costs of the separate handling and storage of the mineral additives were not costs of "treatment processes" which constituted "mining" with respect to the calcium carbonate rock used in producing cement. They were non-mining costs and as such should have been allocated to the denominator of the cost fraction, rather than the numerator, in the proportionate profits computation.

III

THE DISTRICT COURT ERRONEOUSLY EXCLUDED CERTAIN POST-MANUFACTURING COSTS AND INCOME FROM THE COMPUTATION

The errors of the District Court in excluding certain post-manufacturing costs and income from the computation have a common root: the court simply did not apply the proportionate profits method. Instead, it based its ruling on a statutory definition of the mining cutoff point -- a definition irrelevant to the issues. This basic confusion is clear from the orders for preparation of findings, conclusions and judgment. (No. 22,397, I-R. 117-118; No. 22,398, I-R. 170-171.)

In those orders, the court invoked, as controlling, the pre-1960 definition of "mining" as including "ordinary treatment processes" applied "in order to obtain" mineral products in "commercially marketable" form. (Section 613(c)(2) of the 1954 Code, as originally enacted, Appendix A, _infra_, which carried over the definition in Section 114(b)(4)(B) of the 1939 Code, as amended.) The court ruled that this definition required the exclusion of various costs from the proportionate profits computation, including selling expenses and the costs of bags and bagging, because they were incurred "_after_ the products were _obtained_ in 'commercially marketable' form". In support of this ruling, the court cited the Supreme Court's decisions in _Cannelton_ and _Monolith_. The court held

that the first "commercially marketable" product of the corporations' cement-producing operations was bulk cement only, notwithstanding the fact that the finished cement was sold both in bulk and in bags; and, in addition to excluding selling expenses and costs of bags and bagging, it excluded income from the sales of bagged cement from the computation. (No. 22,397, I-R. 124-125; No. 22,398, I-R. 184-185.)

The court's reliance was misplaced. The pre-1960 statutory definition of "mining" and the Cannelton and Monolith decisions had nothing whatever to do with how an integrated producer's constructive income from mining should be computed. Cannelton and Monolith made it clear that an integrated producer is entitled to depletion only on his constructive income from the raw mineral product of "mining". And these decisions defined the mining cutoff point as being reached when the raw mineral product of "mining" is ready for industrial use or consumption -- that is, when a non-integrated miner would be ready to ship and sell his product. The Supreme Court treated the integrated producer as selling his raw mineral to himself at the mining cutoff point.

While Cannelton and Monolith dealt with the pre-1960 statutory definition of "mining", they are equally applicable to the mining cutoff point for calcium carbonate rock prescribed by Section 613(c)(4)(F), Appendix A, infra, as added in 1960 and applicable to

the taxable years here involved. Thus the integrated cement producer's depletable mining income, under Section 613(c)(4)(F), is his constructive income from kiln feed when it is ready for industrial use and consumption; at that point, he is deemed to sell it to himself for manufacture.

But the statute and the cited decisions provide only the context and points of reference for the computation; they do not provide the least intimation as to how the computation is to be made. For more than 25 years, the method of computation for integrated industries prescribed by regulation has been the proportionate profits method. That method is wholly consonant with the statute and with _Cannelton_ and _Monolith_. Under the statute, the depletion allowance is a percentage of income. _Cannelton_ and _Monolith_ limit an integrated producer to depletion on his constructive _income_ from constructive sales of the mining product to himself. Under the proportionate profits method, logically, this constructive income is derived from actual figures: the integrated producer's actual gross income from sales of its manufactured products and its actual costs of producing and selling those products.

The District Court was mistaken on another score. The pre-1960 statutory definition of "mining" did not deal with processes which produced a "commercially marketable" _manufactured_ product -- only with processes which produced a raw mineral ready for industrial

use and consumption. The District Court, however, misconstrued "ordinary treatment processes" as including manufacturing processes, and then concluded that finished bulk cement was the first "commercially marketable" product -- under a definition of "mining". This is confusion worse confounded.

As prescribed in the regulation, the proportionate profits method also refers, of course, to processes and marketability. But the total cost and income figures to be allocated are not measured by reference to mining and manufacturing processes only, or to some abstract valuation of the manufactured product, independent of sales. The income figure to be allocated between mining and non-mining, under the method, is "the representative market or field <u>price</u> of the first marketable product resulting from <u>any</u> process or processes". [Emphasis supplied.] In practice, as noted, the "price" thus allocated is usually the integrated producer's actual gross sales. And an undistorted allocation of the gross sales is achieved only by including, in the cost fraction, every dollar of costs which produced sales. This is precisely what the regulation requires. It is plainly framed in terms of all the costs underlying the <u>price</u> at which the manufactured product is sold, and provides for an allocation of that price to non-mining in proportion to the costs of all "processes <u>beyond</u> the ordinary treatment [mining] processes" -- not just manufacturing processes. [Emphasis supplied.]

As the Court of Claims said in Standard Lime and Cement Co. v. United States, supra, p. 944, "each dollar of costs expended to produce and sell the end product" must be taken into account as earning the same percentage of the profit.

Neither in logic nor on any other ground is there warrant for any other construction of the method's treatment of post-mining costs, i.e., the costs of "processes" beyond mining processes. Among a variety of definitions, Webster defines a "process" broadly as: "A series of actions or operations definitely conducing to an end". This definition is more than ample to cover all of taxpayer's post-manufacturing "actions or operations definitely conducing" to the sales of its manufactured product. In Standard Lime the court referred (329 F. 2d, p. 946) to both manufacturing and marketing as post-mining processes. The reference in Section 613(c)(4)(F) to post-mining processes ("any subsequent process") must be read as broadly embracing both manufacturing and marketing activities, if it is to accord with the statutory requirements for depletion.

In the Senate debates on the so-called Gore amendment, Section 302(b) of the Public Debt and Tax Rate Extension Act of 1960, Appendix A, infra, which added the new definitions of mining to Section 613(c)(4), Senatore Gore stated (106 Cong. Record, Part 10, p. 13240):

> To state the question briefly, the proposed amendment changes the definition of "mining" to preclude the interpretation of the term as including operations involved in processing the finished product, the packaging and shipping of the finished product.

All of such non-mining costs of marketing operations must be included in the denominator of the cost fraction, in the proportionate profits computation, in order to secure a proper allocation of gross sales to mining and non-mining income.

A. The District Court erred in excluding the income from sales of bagged cement, and the costs of bags and bagging, from the computation

For the reasons given above, the District Court erred in excluding the costs of bags and bagging from the computation. By the same token, the court erred in excluding the income from sales of bagged cement. The first "marketable product" was finished cement; the finished cement was sold both in bulk and in bags. Bagging was simply a marketing process producing a portion of its actual gross sales.

The District Court's rulings in this respect are in direct conflict with the decision of the Third Circuit in Whitehall Cement Manufacturing Co. v. United States, 369 F. 2d 468. There the taxpayer sold bagged cement for a price which included a premium referable to its additional packaging costs. The premium was less than the packaging costs. The taxpayer contended that it sustained a loss in the amount of the difference between the two, and that

both the income and the costs of this loss operation should be excluded from the proportionate profits computation. The Third Circuit noted that the taxpayer realized a net profit from sales of bagged cement, albeit less than the profit which would have been realized from the sale of the same cement in bulk; and it held that the exclusions urged by the taxpayer would distort the allocation fraction. The court said (p. 474):

> There is implicit in the plaintiff's argument an erroneous assumption that the packaging costs produced only the additional revenue derived from the premiums, and this was less than the costs. The sale of cement in bags was presumably an accommodation to those customers whose particular requirements were such as to make the purchase of cement in bulk commercially unfeasible. The availability of packaged cement was undoubtedly a sales inducement to such customers. It seems reasonable to infer that the profits realized from the sale of packaged cement * * * were attributable at least in part to the packaging costs. We are of the opinion that packaging costs were properly allocable to the non-mining operations. * * * The profits attributable to such costs were similarly allocable.

In the instant case, as in Whitehall, the premium for bagged cement did not cover the packaging costs and the sales of bagged cement were therefore not as profitable as sales of cement in bulk. Nevertheless, as in Whitehall, the sales of bagged cement did produce an over-all profit.(Pltf. Ex. 20 A-D, p. 470.) Such sales met the particular needs of a group of customers and undoubtedly were a sales inducement to purchases by such customers. The proceeds of

such sales were part of the corporations' gross sales, and the costs of bags and bagging were part of the corporations' expenses of marketing their finished cement. To exclude the bag premium from gross sales and the non-mining costs of bags and bagging from the denominator of the cost fraction, in the proportionate profits computation, "would result in a modification of the allocation fraction and consequently an increase of the depletion base". Whitehall Cement Manufacturing Co. v. United States, supra, p. 474.

B. The District Court erred in excluding selling expenses from the computation; they should be included as non-mining expenses in their entirety

During the taxable years, taxpayer and Arizona Portland incurred certain selling expenses with respect to finished cement, consisting primarily of salaries and other expenses of salesmen and membership in various industry trade associations. The District Court ruled that these expenses should be excluded from the computation or, alternatively, allocated between mining and non-mining costs because they benefitted the mining product. (No. 22,397, I-R. 125; No. 22,398, I-R. 185.) We submit that exclusion was error, and that allocation would be equally erroneous.

The expenses involved were part of the costs which produced the gross sales to be allocated between mining and non-mining income and, as such were includible in the proportionate profits

computation. Moreover, they were non-mining costs in their entirety. They were incurred solely to generate sales of the manufactured end product, finished cement. Integrated producers are their own market for their kiln feed, and are deemed under Cannelton to sell it to themselves. But they incur no actual selling expenses in this connection, and there is nothing in the record to show that sales of the finished cement are promoted by reference to some special quality in a producer's kiln feed. Nor is there anything in the record which would indicate, as a basis for allocation, what the selling expenses of an unintegrated kiln feed producer might be.

Taxpayer had a sales department with a staff of 10 to 15 outside salesmen who operated generally throughout the southern California and southern Arizona territory. (Pltf. Ex. 20 A-D, p. 179.) There is no way in logic whereby the salaries and expenses of these salesmen could be referred back to "sales"of kiln feed. By contrast, some general administrative overhead costs are properly allocable between mining and non-mining because they demonstrably benefit both phases of an integrated operation. Thus, where an executive has responsibilities and duties with respect to both phases, his salary may be allocable. No such basis exists for allocating expenses of selling the finished cement.

Indeed, it should be noted that a manufacturer of cement

who buys his kiln feed (such as Blue Diamond in the instant litigation) would incur exactly the same selling expenses as an integrated producer, and would be at a distinct competitive disadvantage if the integrated producer were allowed to inflate its depletion base by allocating a portion of such expenses to mining costs.

In an intangible sense, it may be said that all of an integrated producer's costs indirectly benefit its entire operation. But the Government does not suggest that, for that reason, a portion of recognized mining costs should be allocated to non-mining; no more should the integrated producer be heard to say that costs of marketing the manufactured product should be allocated to mining costs -- certainly not in the absence of a showing of a rational and logical basis for allocation. In the instant case, as in United States Pipe & Foundry Co. v. Patterson, 203 F. Supp. 335, 364 (N.D. Ala.), the taxpayer cannot point to any item of selling expense that is "properly or fairly allocable" to mining.

As the Court of Claims said in Standard Lime and Cement Co. v. United States, supra, p. 946:

> It follows that only those costs incurred for the benefit of the mining operation as particularized by the statutory scheme, can be included. The language of subparagraph (F) of subsection 613(c)(4) demands this conclusion, for it specifically includes all processes up to kiln feed "but not including any subsequent

> processes." We interpret this as excluding any subsequent manufacturing or marketing processes. [Emphasis supplied.]

IV

THE DISTRICT COURT ERRED IN ALLOCATING BETWEEN MINING AND NON-MINING INCOME AN INFLATED GROSS INCOME FIGURE BASED ON LIST PRICES RATHER THAN ON THE ACTUAL RECEIPTS PRODUCED BY THE SO-CALLED DISCOUNT PRICES

The District Court ruled that discounts to customers were offered exclusively for the purpose of inducing prompt payment, not for the purpose of inducing sales, and should not be deducted in determining depletable gross income from mining. (No. 22,397, I-R. 123, 128; No. 22,398, I-R. 182, 189.) In other words, the court ruled that the income figure in the proportionate profits computation should be based on list prices. The Government contends that this ruling is erroneous; that the actual selling prices, producing the actual gross sales receipts, were the so-called discount prices; and that depletable mining income must be derived, under the proportionate profits method, from the "representative * * * price" reflected in the actual receipts.

It is stipulated that, during the taxable years, all of the major cement producers in the Los Angeles marketing area -- including taxpayer -- offered precisely the same discount on precisely the same terms: 20 cents per barrel for payment by the 10th of the month following the invoice date or within 30 days. (No. 22,397, I-R. 113; No. 22,398, I-R. 165.) Mr. Donoghue, the president of

Blue Diamond Company, a large purchaser of finished cement from the taxpayer and other companies, testified (Pltf. Ex. 20 A-D, pp. 137-138):

> Q. You had no doubt that you could get that barrel discount, did you?
>
> A. I believe it was a standard discount for cement companies, at least in the State of California.
>
> Q. Then it had no influence upon your purchasing decisions, did it?
>
> A. From whom we purchased?
>
> Q. Yes, sir.
>
> * * * * *
>
> A. It would be a question of competitive price. It would affect the selling price if there were a cement company that did not offer the 20-cent-a-barrel discount.

Significantly, only a small percentage of the discounts were ever disallowed. For example, during its taxable year ended April 30, 1959, taxpayer allowed discounts totaling $453,072 from the Colton cement plant and $775,565 from the Mojave cement plant, whereas only $347.85 in potential discounts were disallowed. (No. 22,398, I-R. 103, 112.)

The discount was offered on all sales of cement to all customers irrespective of their credit standing. (Pltf. Ex. 20 A-D, p. 223.) By contrast, the small discounts for prompt payment

allowed from taxpayer's Colton lime plant were highly selective and given only on flour-sized ground rock. (Pltf. Ex. 20 A-D, pp. 229-230.)

Whatever the original reasons for the discount, it is abundantly evident from the foregoing stipulated and evidentiary facts that the so-called discount prices were the actual selling prices, set in competition within the industry. The reduction from list prices was a competitive pricing device with too substantial an impact upon the taxpayer's actual receipts to be regarded as anything but a trade discount. The disallowance of the discount to a few delinquent customers, in negligible amounts, does not derogate from that conclusion.

Dr. Taylor, an independent account expert, testified as follows (Pltf. Ex. 20 A-D, pp. 109-110, 112):

> Q. How would you characterize the difference between a trade discount and a cash discount in a normal accounting sense?
>
> A. A trade discount is part of the bargaining of the price to consummate the transaction, and the cash discount, in its essence is given for the purpose of encouraging payment. * * *
>
> *   *   *   *   *
>
> Q. * * * Were the discounts actually allowed a high percentage of sales, in your opinion?
>
> A. Yes.
>
> Q. In the light of the facts and the accounting concepts, how would you characterize the discounts allowed in this case?

A. I think that the plaintiff (and consistent with the total cement industry) has a discount as a price-making device, and it therefore partakes more of the nature of a trade discount than a discount which would be related as a financial function.

We submit, in sum, that the true selling price -- the "representative * * * price", in the language of the regulation -- was the so-called discount price. And the actual gross income received from sales of cement at this price is the income to be allocated between mining and non-mining, under the proportionate profits method.

CONCLUSION

For the reasons stated above, the judgments of the District Court should be reversed.

Respectfully submitted,

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MARCH, 1968.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19, and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: 14th day of March, 1968.

Loyal E. Keir

Assistant United States Attorney.

APPENDIX A

Internal Revenue Code of 1954:

SEC. 611.[7/] ALLOWANCE OF DEDUCTION FOR DEPLETION.

(a) General Rule.--In the case of mines, oil and gas wells, other natural deposits, and timber, there shall be allowed as a deduction in computing taxable income a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under regulations prescribed by the Secretary or his delegate. * * *

*   *   *   *   *

(26 U.S.C. 1964 ed., Sec. 611.)

SEC. 613.[8/] PERCENTAGE DEPLETION.

(a) General Rule.--In the case of the mines, wells, and other natural deposits listed in subsection (b), the allowance for depletion under section 611 shall be the percentage, specified in subsection (b), of the gross income from the property * * *. * * *

7/ Section 23(m) of the Internal Revenue Code of 1939 (26 U.S.C. 1952 ed., Sec. 23), applicable for the taxable years ending April 30, 1953, and 1954, is substantially the same as Section 611(a) of the Internal Revenue Code of 1954.

8/ Section 114(b)(3) and (4) of the Internal Revenue Code of 1939, as amended by Section 145, Revenue Act of 1942, c. 619, 56 Stat. 798; Section 124, Revenue Act of 1943, c. 63, 58 Stat. 21; Section 207, Revenue Act of 1950, c. 994, 64 Stat. 906; and Section 319, Revenue Act of 1951, c. 521, 65 Stat. 452 (26 U.S.C. 1952 ed., Sec. 114), applicable for the taxable years ending April 30, 1953, and 1954, is substantially the same as Section 613 of the Internal Revenue Code of 1954.

(b) Percentage Depletion Rates.--The mines, wells, and other natural deposits, and the percentages, referred to in subsection (a) are as follows:

* * * * *

(6) 15 percent--all other minerals (including but not limited to * * * limestone * * *), except that * * *

* * * * *

(c) Definition of Gross Income from Property.--For purposes of this section--

(1) Gross income from the property.--The term "gross income from the property" means, in the case of a property other than an oil or gas well, the gross income from mining.

(2) Mining.--The term "mining" includes not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills.

* * * * *

(4) Ordinary treatment processes.--The term "ordinary treatment processes" includes the following:

* * * * *

(26 U.S.C. 1964 ed., Sec. 613.)

SEC. 7807. RULES IN EFFECT UPON ENACTMENT OF THIS TITLE.

(a) Interim Provision for Administration of Title.--Until regulations are promulgated under any provision of this title which depends for its application upon the promulgation of regulations (or which is to be applied in such manner as may be prescribed by regulations) all instructions, rules or regulations which are in effect immediately prior to the enactment of this title shall, to the extent such instructions, rules, or regulations could be prescribed as regulations under authority of such provision, be applied as if promulgated as regulations under such provision.

*   *   *   *   *

(26 U.S.C. 1964 ed., Sec. 7807.)

Public Debt and Tax Rate Extension Act of 1960, P.L. 86-564, 74 Stat. 290:

SEC. 302. DEPLETION RATE FOR CERTAIN CLAYS; TREATMENT PROCESSES CONSIDERED AS MINING FOR COMPUTING PERCENTAGE DEPLETION IN THE CASE OF MINERALS AND ORES.

*　　*　　*　　*　　*

(b) Treatment Processes Considered as Mining.--Subsection (c) of section 613 of the Internal Revenue Code of 1954 (relating to the definition of gross income from property) is amended as follows:

(1) by amending paragraph (2) to read as follows:

"(2) Mining.--The term "mining" includes not merely the extraction of the ores or minerals from the ground but also the treatment processes considered as mining described in paragraph (4) (and the treatment processes necessary or incidental thereto), and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which such treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills."

(2) By striking out paragraph (4) and inserting in lieu thereof the following new paragraphs:

"(4) Treatment processes considered as mining.--The following treatment processes where applied by the mine owner or operator shall be considered as mining to the extent they are applied to the ore or mineral in respect of which he is entitled to a deduction for depletion under section 611:

"(A) In the case of coal--cleaning, breaking, sizing, dust allaying, treating to prevent freezing, and loading for shipment;

"(B) in the case of sulfur recovered by the Frasch process--cleaning, pumping to vats, cooling, breaking, and loading for shipment;

"(C) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and ores or minerals which are customarily sold in the form of a crude mineral product--sorting, concentrating, sintering, and substantially equivalent processes to bring to shipping grade and form, and loading for shipment;

"(D) in the case of lead, zinc, copper, gold, silver, uranium, or fluorspar ores, potash, and ores or minerals which are not customarily sold in the form of the crude mineral product--crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore or the mineral or minerals from other material from the mine or other natural deposit;

"(E) the pulverization of talc, the burning of magnesite, the sintering and nodulizing of phosphate rock, and the furnacing of quicksilver ores;

"(F) in the case of calcium carbonates and other minerals when used in making cement--all processes (other than preheating of the kiln feed) applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process;

"(G) in the case of clay to which paragraph (5) (B) of subsection (b) applies--crushing, grinding, and separating the mineral from waste, but not including any subsequent process; and

"(H) any other treatment process provided for by regulations prescribed by the Secretary or his delegate which, with respect to the particular ore or mineral, is not inconsistent with the preceding provisions of this paragraph.

"(5) Treatment Processes Not Considered as Mining.--Unless such processes are otherwise provided for in paragraph (4) (or are necessary or incidental to processes so provided for), the following treatment processes shall not be considered as 'mining': electrolytic deposition, roasting, calcining, thermal or electric smelting, refining, polishing, fine pulverization, blending with other materials, treatment effecting a chemical change, thermal action, and molding or shaping.

(c) Effective Date.--The amendments made by subsections (a) and (b) shall be applicable only with respect to taxable years beginning after December 31, 1960.

Act of September 14, 1960, P.L. 86-781, 74 Stat. 1017:

SEC. 4. Subsection (c) of section 302 of the Public Debt and Tax Rate Extension Act of 1960 (Public Law 84-564; 74 Stat. 293) is amended to read as follows:

"(c) Effective Date.--

"(1) In general.--Except as provided in paragraph (2), the amendments made by subsections (a) and (b) shall be applicable only with respect to taxable years beginning after December 31, 1960.

(2) Calcium carbonates, etc.--

(A) Election for past years.--In the case of calcium carbonates or other minerals when used in making cement, if an election is made by the taxpayer under subparagraph (C)--

"(i) the amendments made by subsection (b) shall apply to taxable years with respect to which such election is effective, and

"(ii) provisions having the same effect as the amendments made by subsection (b) shall be deemed to be included in the Internal Revenue Code of 1939 and shall apply to taxable years with respect to which such election is effective in lieu of the corresponding provisions of such Code.

"(B) Years to which applicable.--An election made under subparagraph (C) to have the provisions of this paragraph apply shall be effective for all taxable years beginning before January 1, 1961, in respect of which--

"(i) the assessment of a deficiency,
"(ii) the refund or credit of an overpayment,

or

"(iii) the commencement of a suit for recovery of a refund under Section 7405 of the Internal Revenue Code of 1954,

is not prevented on the date of the enactment of this paragraph by the operation of any law or rule of law. Such election shall also be effective for any taxable year beginning before January 1, 1961, in respect of which an assessment of a deficiency has been made but not collected on or before the date of the enactment of this paragraph.

(C) Time and manner of election.--An election to have the provisions of this paragraph apply shall be made by the taxpayer on or before the 60th day after the date of publication in the Federal Register of final regulations issued under authority of subparagraph (F), and shall be made in such form and manner as the Secretary of the Treasury or his delegate shall prescribe by regulations. Such election, if made, may not be revoked.

"(D) Statutes of limitation.--Notwithstanding any other law, the period within which an assessment of a deficiency attributable to the application of the amendments made by subsection (b) may be made with respect to any taxable year to which such amendments apply under an election made under subparagraph (C) and the period within which a claim for refund

or credit of an overpayment attributable to the application of such amendments may be made with respect to any such taxable year, shall not expire prior to one year after the last day for making an election under subparagraph (C). An election by a taxpayer under subparagraph (C) shall be considered as a consent to the application of the provisions of this subparagraph.

"(E) Terms; applicability of other laws.--Except where otherwise distinctly expressed or manifestly intended, terms used in this paragraph shall have the same meaning as when used in the Internal Revenue Code of 1954 (or corresponding provisions of the Internal Revenue Code of 1939) and all provisions of law shall apply with respect to this paragraph as if this paragraph were a part of such Code (or corresponding provisions of the Internal Revenue Code of 1939).

"(F) Regulations.--The Secretary of the Treasury or his delegate shall prescribe such regulations as may be necessary to carry out the provisions of this paragraph."

Treasury Regulations on Income Tax (1954 Code):

Sec. 1.9003-2
Effect of election.

(a) In general. If a taxpayer makes the election described in paragraph (b) of Section 1.9003-1, he shall be deemed to have consented to the application of section 302(b) of the Act with respect to all taxable years to which the election applies. Thus, subparagraph (F) of section 613(c)(4) of the Internal Revenue Code of 1954 as amended must be applied in determining gross income from mining for the taxable years to which the election applies (including years subject to the Internal Revenue Code of 1939) whether or not the taxpayer is litigating the issue. Further, the election shall apply to all calcium carbonates or other minerals mined and used by the taxpayer in making cement.

(b) Effect on gross income from mining. The election is only determinative of what constitutes "mining" for the purposes of computing percentage depletion and has no effect on

the method employed in determining the amount of gross income from mining. In applying the election to the years affected there shall be taken into account the effect that any adjustments resulting from the election shall have on other items affected thereby, such as charitable contributions, foreign tax credit, net operating loss, and the effect that adjustments to any such items shall have on other taxable years. The provisions of section 302(b) of the Act are applicable with respect to taxable years subject to the Internal Revenue Code of 1939 for purposes of applying section 450 and 453 of that Code.

(26 C.F.R. Sec. 1.9003-2.)

Treasury Regulations 118 (1939 Code):

Sec. 39.23(m)-1. Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.

* * * * *

(e) As used in section 114(b)(3) and 114(b)(4)(A) and section 39.23(m)-1 to 39.23(m)-19, inclusive, the term "gross income from the property" means the following:

* * * * *

(3) If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold, but, if the product is transported or processed (other than by the ordinary treatment processes described below) before sale, "gross income from the property" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes actually applied, before transportation of such product (other than transportation treated, for the taxable year, as mining).

If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude mineral state is merely transported the price for which sold) minus the costs and proportionate profits attributable to the transportation (other than transportation treated, for the taxable year, as mining) and the processes beyond the ordinary treatment processes. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

* * * * *

H. Conference Rep. No. 2005, 86th Cong., 2d Sess., pp. 8-11 (1960-2 Cum. Bull. 741, 746-747):

<u>Treatment processes considered as mining</u>

* * * * *

Paragraph (2) of section 302(b) added to the bill under the conference agreement strikes out paragraph (4) of section 613(c) of the 1954 Code and inserts in lieu thereof new paragraphs (4) and (5).

<u>Specifically included treatment processes</u>.-- The new paragraph (4) of section 613(c) describes (in subpars. (A) to (H), inclusive) treatment processes which are to be considered as mining, where applied by the mineowner or operator, to the extent such processes are applied to the ore or mineral in respect of which the mine owner or operator is entitled to a deduction for depletion under section 611 of the 1954 Code. As under existing law, a described process is to be treated as mining where performed by another person for the mineowner or operator if the mineowner or operator has not disposed of his depletable interest in the ore or mineral to which such process is applied. Under the language of this provision, a described process is not treated as mining where applied to a purchased ore or mineral.

* * * * *

For calcium carbonates and other minerals when used in making cement, a new subparagraph (F) has been added providing for the allowance of all processing up to the point of the introduction of the kiln feed into the kiln (except for preheating of the kiln feed), but not including any subsequent process. * * *

Specifically excluded treatment processes.--The new paragraph (5) added to section 613(c) of the 1954 Code under the conference agrement provides that unless such processes are otherwise provided for in paragraph (4) (or are necessary or incidental to processes so provided for), the following treatment processes shall not be considered as "mining": electrolytic deposition, roasting, calcining, thermal or electric smelting, refining, polishing, fine pulverization, blending with other materials, treatment effecting a chemical change, thermal action, and molding or shaping.

*　　*　　*　　*　　*

H. Conference Rep. No. 2213, 86th Cong., 2d Sess., p. 4 (1960-2 Cum. Bull. 902, 904):

ELECTION AS TO BASE FOR DETERMINATION PERCENTAGE DEPLETION DEDUCTION IN THE CASE OF MINERALS USED IN MAKING CEMENT

Amendment No. 1: To determine the percentage depletion allowance under present law, it is necessary to multiply the percentage rate applicable to the particular mineral by the value of the mineral at the point at which the mining process ends. This point is referred to as the "cutoff point." In the case of many mineral industries, this cutoff point has been the subject of uncertainty and litigation. Included in this group is the cement industry.

In order to resolve the cutoff question for 1961 and future years, Congress in the Public Debt and Tax Rate Extension Act of 1960 modified section 613(c) of the Internal Revenue Code of 1954. As amended, this statutory provision established specific cutoff points for numerous minerals, including those used in the manufacture of cement. This cutoff point for cement-producing minerals (except for preheating of the kiln feed) occurs just prior to the introduction of the kiln feed into the kiln. This cutoff point is derived from a ruling published by the Treasury Department in 1953.

Although the recent legislation determines the cutoff point for the cement industry for future years, it does not settle this question for any open years prior to 1961. Senate amendment No. 1 permits taxpayers mining minerals used in making cement to elect to apply, for the years prior to 1961, the cutoff provisions adopted in the Public Debt and Tax Rate Extension Act of 1960. If a taxpayer fails to make the election, the cutoff point in his case for these years would be determined under existing law.

Under the amendment, if the taxpayer makes the election, it will apply to all of his mineral properties used in making cement and, in general, to all of his taxable years beginning before 1961 which are open on the date of the enactment of the bill. However, the making of the election resolves only the point at which the cutoff occurs and does not deal with any other matters which may be in issue, such as the method of computing the gross income at that point. The election must be made by the taxpayer on or before the date which is 60 days after the date of the publication of final regulations on this provision. Once made, the election is irrevocable.

*   *   *   *   *

APPENDIX B

TABLE OF EXHIBITS PURSUANT TO RULE 18(2)(5) AS AMENDED:

Exhibit	Identified	Offered	Received
Pltf. Ex. 1	II-R. 66 [9/]	II-R. 73	II-R. 73
Pltf. Ex. 4	II-R. 67	II-R. 73	II-R. 73
Pltf. Ex. 5	II-R. 68	II-R. 73	II-R. 73
Pltf. Ex. 6	II-R. 68	II-R. 73	II-R. 73
Pltf. Ex. 7	II-R. 68	II-R. 73	II-R. 73
Pltf. Ex. 8	II-R. 69	II-R. 73	II-R. 73
Pltf. Ex. 9	II-R. 70	II-R. 73	II-R. 73
Pltf. Ex. 10	II-R. 70	II-R. 73	II-R. 73
Pltf. Ex. 11	II-R. 70	II-R. 73	II-R. 73
Pltf. Ex. 12	II-R. 70	II-R. 73	II-R. 73
Pltf. Ex. 13	II-R. 71	II-R. 73	II-R. 73
Pltf. Ex. 14	II-R. 71	II-R. 73	II-R. 73
Pltf. Ex. 19	II-R. 74	II-R. 74	II-R. 74
Pltf. Ex. 20A-D	II-R. 75	II-R. 75	II-R. 76
Pltf. Ex. 24	II-R. 78	II-R. 78	II-R. 79
Pltf. Ex. 25	II-R. 79	II-R. 79	II-R. 79
Deft. Ex. A	II-R. 115-116	II-R. 115-116	II-R. 116
Deft. Ex. B	II-R. 115-116	II-R. 115-116	II-R. 116
Deft. Ex. C	II-R. 115-116	II-R. 115-116	II-R. 116

9/ "II-R." refers to the Reporter's Transcript of proceedings held on November 10, 1966, and January 24, 1967.

Nos. 22397-22398-A

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

No. 22397

UNITED STATES OF AMERICA,

Appellant,

vs.

CALIFORNIA PORTLAND CEMENT COMPANY, a corporation, Successor-in-Interest to ARIZONA PORTLAND CEMENT COMPANY, a corporation,

Appellee.

No. 22397-A

CALIFORNIA PORTLAND CEMENT COMPANY, a corporation, Successor-in-Interest to ARIZONA PORTLAND CEMENT COMPANY, a corporation,

Cross-Appellee,

vs.

UNITED STATES OF AMERICA,

Cross-Appellant.

No. 22398

UNITED STATES OF AMERICA,

Appellant,

vs.

CALIFORNIA PORTLAND CEMENT COMPANY,

Appellee.

No. 22398-A

CALIFORNIA PORTLAND CEMENT COMPANY,

Cross-Appellant,

vs.

UNITED STATES OF AMERICA,

Cross-Appellee.

Opening Brief for California Portland Cement Company.

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TOPICAL INDEX

TABLE OF AUTHORITIES CITED

Statutes and Regulations

Nos. 22397-22398A

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CALIFORNIA PORTLAND CEMENT COMPANY,

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UNITED STATES OF AMERICA,

Cross-Appellee.

Opening Brief for California Portland Cement Company.

Jurisdiction.

These consolidated civil actions for refund of Federal income and excess profits taxes were duly commenced in the District Court for the Central District of California, under Sections 1346(a)(1) and 1402(a)(1) of Title 28 of the United States Code. The judgments of the District Court became final on July 31, 1967.[1] The Government filed its appeal on September 28, 1967,[2] and California Portland cross-appealed on October 6, 1967.[3] The jurisdiction of this Court rests upon Section 1291 of Title 28 of the United States Code.

Statutes and Regulations Involved.

The pertinent provisions of the statutes and Treasury Regulations involved are reproduced in Appendix A.

Statement of the Case.

These consolidated cases[4] involve the claims of California Portland Cement Company ("California Portland"), individually and as successor-in-interest to its former wholly-owned subsidiary, Arizona Portland Cement Company ("the Arizona Company"), for refund of a portion of the Federal income and excess profits taxes paid to the Government for the taxable years 1953-59.[5] The basic issue is the proper compu-

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[1]No. 22397, I-R. 162; No. 22398, I-R. 237.

[2]No. 22397, I-R. 163; No. 22398, I-R. 238.

[3]No. 22397, I-R. 165; No. 22398, I-R. 240.

[4]By Order of this Court entered January 11, 1968, the within cases were consolidated for purposes of briefing, argument, and decision.

[5]No. 22398 involves returns filed by California Portland with respect to its Colton Quarry and its Mojave Quarry (commencing in the taxable year ended April 30, 1956) for the taxable years ended April 30, 1953 through April 30, 1959, inclusive. [No. 22398, I-R. 177-78] No. 22397 involves returns filed by the Arizona Company with respect to its Rillito Quarry for the taxable years ended April 30, 1953 through April 30, 1957, inclusive. [No. 22397, I-R. 121]

tation of the Federal income tax percentage depletion allowance with respect to calcium carbonate rock extracted from the taxpayers' limestone quarries and processed into Portland cement.

During the period concerned, calcium carbonate rock was extracted by California Portland from its quarries located at Colton and Mojave, California, and by the Arizona Company from its quarry located at Rillito, Arizona, and processed by said companies into finished cement (Portland and allied types.)[6] The calcium carbonate rock at all the quarries had substantially the same physical, chemical and mineral properties, and was processed into the same product of finished cement by application of the same processes at each cement plant as follows: quarrying, crushing, raw grinding together with additives, storage of the resultant kiln-feed in silos, burning and sintering in rotary kilns to produce cement clinker, finish grinding of the cement clinker after the addition of gypsum and sometimes other additives, and storage of the resultant finished bulk cement in silos.[7] A portion of the finished cement was later placed in sacks, and all of such cement, both in bulk and in sacks, was loaded for shipment.[8]

In an action captioned *California Portland Cement Co. v. R. A. Riddell, District Director of Internal Revenue* (No. 138-58 W.M., Civil, decided February 16, 1965 and herein called "the 1951-52 Case"),[9] the present

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[6]No. 22397, I-R. 121; No. 22398, I-R. 177-78.

[7]No. 22397, I-R. 80-82; No. 22398, I-R. 116-19.

[8]No. 22397, I-R. 81; No. 22398, I-R. 116.

[9]The 1951-52 Case was formally heard by this Court on two separate occasions, in Nos. 16438 and 18506 of the files of this Court. The opinions of this Court are reported at 297 F.2d 345 (1962) and 330 F.2d 16 (1964). Citations to proceedings in the 1951-52 Case shall be made throughout this brief. This Court may take judicial notice of said prior proceedings and of the materials in its files. *Gullo v. Veterans Housing Assn.*, 269 F.2d 517 (D.C. Cir. 1959); *Hicks v. Holland,* 235 F.2d 183 (6th Cir. 1956), ***cert. den.*** 352 U.S. 855 (1956).

parties litigated the proper depletion computation method with respect to California Portland's Colton Quarry[10] for the immediately preceding taxable years 1951-52. The 1951-52 Case determined (i) the depletion base against which the pertinent calcium carbonates percentage depletion rate[11] was to be applied (the constructive value of the kiln feed prior to introduction into the kiln), and (ii) the method of arriving at such constructive value.[12]

The facts with respect to the quarrying and cement producing operations at the Colton Quarry during the taxable years 1953-59 are in all material respects identical to the facts determined in the 1951-52 Case.[13] Similarly, the facts with respect to the quarrying and cement producing operations at the Mojave and Rillito Quarries during the years concerned[14] are also identical in all material respects to the facts determined in the 1951-52 Case.[15]

In the proceedings below, California Portland contended that the depletion computation method determined in the 1951-52 Case should be applied for the years 1953-59 because (i) the Government had had its day in court and should be collaterally estopped from relitigating the merits of the 1951-52 Case, and (ii) the 1951-52 Case had been correctly decided and was *stare*

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[10] As used herein, the term "quarry" shall include both the quarry itself and the nearby rock processing and cement plant.

[11] The percentage depletion rate allowed for calcium carbonates was 10% for the years concerned in the 1951-52 Case and for the first year and 245/365ths involved in the present case. For periods thereafter, the allowable rate was 15%. See, e.g., No. 22398, I-R. 188.

[12] The complete text of the final decision in the 1951-52 Case is unofficially reported at 66-2 USTC para. 9624. The official text of said decision is contained at R. 5-36 (particularly 23-36) in No. 18506, as amended by Pltf. Ex. 9 herein.

[13] No. 22398, I-R. 117, 185-86.

[14] 1956-59 for Mojave and 1953-57 for Rillito.

[15] N. 13, *supra;* No. 22397, I-R. 81, 125-26.

decisis. The Government did not question that the purpose of the depletion computation was to arrive at a constructive value of the kiln feed, but argued that the method of arriving at such constructive value should be different from that determined in the 1951-52 Case.

The District Court held that the depletion computation method determined in the 1951-52 Case should be applied in the present case.[16] California Portland has cross-appealed from this decision for protective purposes only, and seeks to depart from the 1951-52 Case computation only if this Court does not affirm the District Court.

Questions Presented.

1. Is the Government collaterally estopped from attacking in this proceeding the depletion computation method determined in the 1951-52 Case?

2. Was the District Court correct in applying for the taxable years 1953-59 the same depletion computation method determined for the immediately preceding taxable years in the 1951-52 Case?

3. If the District Court is not affirmed by this Court, should loading costs be treated in accordance with California Portland's alternative contention?

Specification of Error for California Portland's Cross-Appeal.

1. California Portland believes that the 1951-52 Case should dispose of the instant litigation, and that the District Court's reliance thereon was correct. At the trial, however, California Portland advanced an alternative position with respect to treatment of loading

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[16]Compare the computation method for each year here concerned as specified at I-R. 131-46 in No. 22397 and I-R. 192-224 in No. 22398, with the 1951-52 Case computation method set forth at R. 5-36 (particularly 23-36) in No. 18506, as amended by Pltf. Ex. 9 herein.

costs. Said alternative was not adopted by the District Court, and California Portland alleges that this was error only in the event that this Court does not affirm the computation method adopted by the District Court below and in the 1951-52 Case.

Summary of Argument.

The Government insists on relitigating for 1953-59 the identical depletion computation established in the 1951-52 Case. We believe such relitigation is inequitable, an unwarranted burden on the courts and California Portland, and foreclosed by the principle of collateral estoppel. Accordingly, we submit that this principle provides the first basis for affirmance of the judgment of the District Court.

Assuming *arguendo* that it is proper to reach the merits, we further submit that the District Court's refusal to change the computational method developed after seven years of litigation in the 1951-52 Case was clearly correct.

The Government's position that the costs and revenues of sacked cement should be included in the depletion computation ignores the express "first marketable product" requirement of the pertinent Regulation, results in *two* constructive prices for a single, fungible product—kiln feed, and disregards the great preponderance of the judicial authorities.

The Government's argument that selling expenses do not benefit the entire mining-manufacturing operation of an integrated taxpayer ignores common sense, its own Regulations, and controlling precedent. This position also disregards the entire purpose of the depletion computation, which is to construct a hypothetical sales price for kiln feed equal to that which would be charged by a nonintegrated producer of that product.

With respect to cash discounts, the Government disregards the express findings of the District Court pertaining to their nature and purpose in the present case. The Government also ignores the fact that its own principal judicial authority is in complete accord with the 1951-52 Case and the District Court's judgment on this point.

The final question raised by the Government's appeal involves the costs of storage and handling certain prekiln additives, and is *de minimus*. Contrary to the Government's contention, we believe this cost is clearly necessary and incidental to the blending of such additives with California Portland's in-process calcium carbonate rock.

There is authority for treatment of California Portland's loading and shipping costs on a basis more favorable to it than the treatment prescribed in the 1951-52 Case and by the District Court. Although this alternative treatment would result in a substantial tax refund, California Portland seeks to depart from the 1951-52 Case computation only if this Court does not affirm the District Court.

ARGUMENT.

I.

THE GOVERNMENT IS COLLATERALLY ESTOPPED FROM ATTACKING THE JUDGMENT OF THE DISTRICT COURT.

To simplify our discussion of the collateral estoppel issue, we shall analyze the circumstances pertaining to California Portland's Colton Quarry during the taxable years 1951-52, and during the immediately succeeding taxable years 1953-59.[17]

As mentioned previously, the facts pertaining to the extraction and processing of calcium carbonate rock into finished cement and the sale thereof (as well as all other material facts) at the Colton Quarry were unchanged during the entire period 1951-59.[18] The parties and depletion computation issue in the present case are identical with those in the 1951-52 Case,[19] and, with respect to the Colton Quarry, the single difference in the present case from the 1951-52 Case is the circumstance that different taxable years are involved. The depletion computation method determined in the 1951-52 Case resulted from a litigation which required more than seven years to conclude, and involved three trials in the District Court and three appeals to this Court.[20] Under well established principles of col-

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[17]This accords with the way in which the cases were briefed and argued below. See, e.g., Gov't. Op. Tr. Br. 3, n. 1.

[18]See n. 13, *supra.*

[19]See, e.g., n. 16, *supra.*

[20]See I-R. and II-R. in No. 16438, at 160-778; R. in No. 18506 at 49-169; Pltf. Ex. 8; 297 F.2d 345 (1962); 330 F.2d 16 (1964); Pltf. Ex. 9 and 10. Suit was commenced in the 1951-52 Case on February 13, 1958, and was not concluded until May 25, 1965, when the Government's appeal to this Court from the District Court's judgment entered February 16, 1965 was dismissed.

lateral estoppel, the Government should not be permitted to relitigate for 1953-59 the depletion computation method which was so painstakingly determined for 1951-52. See, e.g., *Commissioner v. Sunnen*, 333 U.S. 591 (1948);[21] *Tait v. Western Maryland Ry. Co.*, 289 U.S. 620, 623 (1933); *Union Bag-Camp Paper Corp. v. United States*, 366 F.2d 1011 (Ct. Cl. 1966).

(a) The Alleged Compromise.

In argument below, the Government attempted to justify its present relitigation by claiming that, despite the three trials and three appeals in the prior case, that case was not determined on the merits but instead was compromised by private agreement.[22] The record in the 1951-52 Case establishes that this simply is not true.

The first trial in the 1951-52 Case was held before Judge Mathes in the then Southern District of California during October 16-23, 1958.[23] The two primary issues were (i) the nature of California Portland's Colton mineral deposit and (ii) the appropriate method of computing its percentage depletion allowance. Within the latter issue were subsidiary questions such as the treatment of cash discounts and of expenses and revenues attributable to the sale of a portion of California Portland's cement in sacks rather than in bulk.[24]

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[21]". . . [M]atters which are actually litigated and determined in the first proceeding cannot later be relitigated. Once a party has fought out a matter in litigation with the other party, he cannot later renew that duel . . . . Collateral estoppel operates, in other words, to relieve the government and the taxpayer of 'redundant litigation of the identical question of the statute's application to the taxpayer's status.'" *Commissioner v. Sunnen, supra.*, 333 U.S. at 598, 599.

[22]See, e.g., Gov't. Op. Tr. Br. 26-29.

[23]II-R. in No. 16438 at 780-81.

[24]I-R. in No. 16438 at 130-52, particularly Findings 13, 14 and 26 at 138-39, 143-44.

The District Court's Findings, Conclusions, and Judgment in the first trial determined (i) that the Colton mineral deposit consisted of calcium carbonates rather than marble,[25] (ii) that California Portland's depletion base was the value of its finished cement,[26] and (iii) the proper treatment of cash discounts, sacking, and certain "additives" in the depletion computation.[27] The Government appealed said judgment to this Court, alleging error in the District Court's classification of the mineral deposit, allowance of the value of finished cement as the depletion base, and treatment of sacking and additives in the depletion computation. The Government did not contest the District Court's treatment of cash discounts in the computation.[28]

While the first appeal in the 1951-52 Case was pending before this Court, the United States Supreme Court decided *United States v. Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960); Congress enacted Public Laws 86-564 (74 Stat. 290) and 86-781 (74 Stat. 1017); and California Portland made a timely election to have all open taxable years governed by such legislation. The net result was that California Portland's depletion computation was required to construct a value of its mineral product at the processing point of introduction of the kiln feed into the kiln, rather than at the point of finished product sale. This Court affirmed the District Court's classification of the Colton mineral deposit, and, in view of California Portland's election of treatment under Public Law 86-564, remanded the cause for the District Court's determination of the proper deple-

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[25]I-R in No. 16438 at 137.

[26]*Id.* at 143-44 (Findings 26 and 27).

[27]*Id.* at 139, 144 (Findings 14 and 26), 138-39, 144 (Findings 13 and 26) and 139 (Finding 15).

[28]II-R. in No. 16438 at 786-87.

tion computation method using the new kiln feed cut-off point.[29]

At the second trial the District Court entered new findings and conclusions which defined a depletion computation method using the kiln feed cut-off point and which, in particular, (i) re-entered the unappealed treatment of cash discounts developed at the first trial,[30] (ii) excluded the costs and revenues of sacking cement from the computation,[31] and (iii) specified the treatment in said computation of certain pre-kiln additives.[32] The Government again appealed to this Court, alleging as error only the District Court's treatment of pre-kiln additives in its revised depletion computation.[33] The Government again did not appeal from the District Court's treatment of cash discounts, nor did it appeal from the treatment of sacking or any other aspect of the District Court's second trial depletion computation apart from the treatment of pre-kiln additives.[34]

On appeal, the Government conceded that the cost of blending pre-kiln additives with the calcium carbonate rock was a "mining" cost, and the point considered by this Court was restricted to the narrow question of whether the acquisition cost of such additives was also a "mining" cost. This Court resolved this point in favor of the Government, and the case was again remanded to the District Court.[35]

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[29]*Riddell v. California Portland Cement Co.,* 297 F.2d 345 (9th Cir. 1962).

[30]R. 12, 18 in No. 18506 (Findings 13 and 29).

[31]*Id.* at 17 (Finding 28).

[32]*Id.* at 12, 18 (Findings 14 and 29).

[33]*Id.* at 171.

[34]*Ibid.*

[35]*Riddell v. California Portland Cement Co.,* 330 F.2d 16 (9th Cir. 1964).

At the third proceeding before the District Court, the parties represented that the single substantive question remaining was the treatment in the depletion computation of the cost of storing and handling pre-kiln additives on the taxpayer's premises, after acquisition but prior to blending with the calcium carbonate rock.[36] Because of the small amount involved, and to avoid a separate trial on this point alone, the Government was willing to concede to California Portland's treatment of such cost.[37] It did not want to be bound by such concession for future years, however, because what was then a *de minimus* question might subsequently achieve financial importance.[38] Accordingly, the Government proposed that the parties stipulate to a dollar amount of judgment, and not request the District Court to make any findings of fact or conclusions of law.[39] This procedure was unacceptable to counsel for California Portland, however, because he wished to make binding for future years all of the elements of the depletion computation which had been litigated, judicially determined, and not appealed. California Portland's counsel specifically stated that he did not wish the entire previous litigation and judicial determinations to be nullified for collateral estoppel purposes merely because of a compromise at the third proceeding on one small point.[40] Judge Mathes stated that the second trial

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[36]Pltf. Ex. 8, pp. 5-6, 11-16.

[37]*Id.* at 5-6.

[38]*Id.* at 16.

[39]*Id.* at 5-6, 10, 16.

[40]"MR. PEELER: Your Honor, the plaintiff has this problem: As you recall, this is, in effect, the third trial. We have had a series of Government counsel, each of whom, with all due respect, has had new ideas as to depletion. We have some twelve taxable years subsequent to the years in suit which presumably are governed by the principles of this litigation.

"We would hardly be anxious to settle this case just on a money-judgment basis, and then be faced with another seven or

findings and conclusions which had not been appealed could no longer be disputed, and that he would reenter all such unappealed findings and conclusions.[41] On this basis, discussion between the Court and counsel resulted in the suggestion that the parties stipulate to a reentry of the Court's unappealed second trial findings and conclusions, and that the Government expressly reserve its right to relitigate the treatment of handling costs of pre-kiln additives.[42] The Government's attorney stated that he thought the unappealed findings and conclusions were still valid and that updated findings and conclusions would not be necessary.[43] He was agreeable, however, to the above suggested proce-

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eight years of trial on the later years. In other words, those matters which are resolved in this action, such as the sacking and the discounts, we want to treat as finally resolved for all times; unless the Government can show a material change in the facts for later years.

"THE COURT: Well, those items cannot be disputable.

"MR. PEELER: We hope they are no longer in dispute.

"MR. SCHWALB: No longer in dispute for this case. They were decided by your Honor, and not appealed.

"MR. PEELER: In other words, the plaintiff's position, your Honor, is this: That we are entitled in any final decision by this court to have definitive findings of fact and conclusions of law.

"Now, as to some 95 per cent of the findings and conclusions entered by this court at the time of the second trial there either was no appeal to the Ninth Circuit, or there was a concession before the Ninth Circuit, so that those findings and conclusions should still stand as is.

"All we are asking is that they be updated to reflect the decision of the Ninth Circuit; and further that the computations, the schedule computing depletion allowance and refund which were made a part of earlier findings have substituted for them the new computations that we have submitted to the Government at this stage." Pltf. Ex. 8, pp. 7-8.

[41]"THE COURT: Well, those items [referring to previously resolved matters such as the treatment of sacking and discounts] cannot be disputable . . . . I would readopt all the findings of fact and conclusions of law that were not expressly appealed from, of course." Pltf. Ex. 8, pp. 7, 20.

[42]Pltf. Ex. 8, pp. 10-11, 16, 17-18.

[43]*Id.* at 10, 16.

dure,[44] but did not wish by his stipulation to deprive the Government of any right which it might otherwise have. If the Government was to be bound by collateral estoppel in future years, he desired that this condition exist as a matter of law rather than as a result of his consent to such effect.[45] The procedure for updating the unappealed second trial findings and conclusions was therefore agreed upon as follows:

> "THE COURT: Let's start this way: Let's incorporate by reference in a new set of findings the certain portion of the findings and conclusions heretofore made that were not appealed from, and then go from there. Where does that leave us? . . . .
>
> "MR. PEELER: . . . [W]e would be willing to accept a limited reservation on the part of the Government that their concession insofar as this intermediate area of the handling costs of the additives prior to the blending concerned is for purposes of this action only and will not be binding in the future.
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> "THE COURT: Won't that meet the situation?
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> "MR. SCHWALB: It does, except my proposed stipulation for judgment and form of judgment accomplish the same purpose.
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> "THE COURT: Except there is always the problem that a reversal and remand, ipso facto, works as a setting aside of all the findings of fact and conclusions of law and judgment . . . .

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[44]*Id.* at 16, 17-18.

[45]"MR. SCHWALB: And although now it doesn't seem, as a matter of law, that we have to be too concerned, nevertheless I wouldn't want it as a matter of record that I have stipulated and that the Government would be so bound. *If the collateral estoppel principle is against us, it will be as a matter of law rather than by my agreement.*" Pltf. Ex. 8, pp. 20-21. (emphasis added)

"MR. SCHWALB: Could we do this to avoid any problem—and I do envision some problem in rewording the findings, and it is just going to prolong it. So would something like this do, a stipulation that those findings and conclusions not appealed from by the Government will stand as the findings and conclusions in this case with respect to all items *other than this one item of purchased additives.* With respect to the purchased additives, X-dollars shall be treated as mining, and Y-dollars be treated as non-mining; and the treatment of X-dollars as mining will not bind the Government for future years . . . .

"MR. PEELER: A stipulation such as just mentioned we could do right now. * * *"[46] (emphasis added)

In accordance with the above procedure, the parties executed and filed in the 1951-52 Case the document which is Plaintiff's Exhibit 9 in this case. Essentially, Exhibit 9 agreed to reentry without change of the unappealed second trial findings of fact and conclusions of law, and made appropriate modifications to the treatment of purchased additives which had been the subject of the second appeal to this Court. Finding 33 of said Exhibit 9 provides in its entirety as follows:

"33. By agreeing to the entry of the foregoing Findings of Fact and the following Conclusions of Law, the defendant has not waived his objections thereto nor does the defendant concede the correctness thereof either for the taxable years in suit or subsequent taxable years. Defendant has stipulated to the entry thereof to avoid another trial for the taxable years involved and so that

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[46]Pltf. Ex. 8, pp. 10-11, 16, 17-19.

final Findings of Fact and Conclusions of Law and a final Judgment may be entered without further delay. As to certain of the costs relating to the handling of additives ($21,390.00 for the taxable year ended April 30, 1951 and $14,321.00 for the taxable year ended April 30, 1952) herein treated as mining costs (see Finding of Fact No. 30, *supra,* Conclusion of Law No. 6, *infra,* and the computations shown in Exhibit A attached hereto), the defendant has not waived his objection thereto nor conceded the correctness thereof but has stipulated to such computations in order that final Findings of Fact and Conclusions of Law, and a final Judgment may be entered for the taxable years in suit without further delay."

The Government now argues that the above procedure constituted a compromise of the entire merits of the 1951-52 Case, and therefore that said case does not collaterally estop it from relitigating the identical matters here. We respectfully submit that the transcript of the third proceeding before Judge Mathes makes it clear that the only compromise on the merits was with respect to the *de minimus* question of the handling cost of pre-kiln additives, and that as to all other substantive matters the parties agreed only to a *procedure* to effect reentry of the unappealed second trial findings and conclusions. The fact that the Government did not compromise or agree to the entire merits of the 1951-52 Case is explicitly stated in Finding 33:

"By agreeing to the entry of the foregoing Findings of Fact and the following Conclusions of Law, the defendant has not waived his objections thereto nor does the defendant concede the correctness thereof *either for the taxable years in suit* or subsequent taxable years. . . ." (emphasis added)

In addition, had there been a compromise of the entire merits, the Government would have had no right to appeal the settlement it had made.[47] On April 14, 1965, however, the Government again made clear that it did not consider the merits of the 1951-52 Case to be concluded by settlement or compromise, and appealed to this Court from the District Court's judgment.[48]

We believe that the foregoing establishes beyond question that the Government's stipulation to the procedure for reentry of the unappealed second trial findings and conclusions represents no more than a variation of the typical case where, after trial and a statement by the trial judge of the way he will rule, the parties agree to the form of findings, conclusions, and judgment, but do not agree on the merits.[49]

In *United States v. International Building Co.*, 345 U.S. 502 (1953), an attempt was made to give collateral estoppel effect to a judgment of the Tax Court which had been entered after a stipulation that there was no deficiency, and without hearing, briefs, or argument. In holding that the parties' agreement on the merits prevented the judgment from having collateral estoppel effect, the Court stated:

> "There is no showing either in the record or by extrinsic evidence [citation omitted] that the issues raised by the pleadings were submitted to the Tax Court for determination or determined by that court. . . . *A judgment entered with the con-*

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[47] See, e.g., *Swift & Co. v. United States*, 276 U.S. 311, 323-24 (1927); Note, *The Consent Judgment as an Instrument of Compromise and Settlement*, 72 HARV. L. REV. 1314, 1323 (1959).

[48] Pltf. Ex. 10.

[49] See, e.g., Local Rule 7(a) of the District Court. Indeed, the very concept of "findings" implies adjudication. See F.R.C.P. 52(a).

> *sent of the parties may involve a determination of questions of fact and law by the court.* But unless a showing is made that that was the case, the judgment has no greater dignity, so far as collateral estoppel is concerned, than any judgment entered only as a compromise of the parties." 345 U.S. at 505-06. (emphasis added)

In the present case, California Portland's entire percentage depletion method was fully litigated and determined at the second trial of the 1951-52 Case. The only facet of such depletion method which then was appealed was the narrow question of the treatment of pre-kiln additives. On remand the Government was not entitled to re-open the unappealed second trial findings and conclusions absent exceptional circumstances,[50] it made no such effort, and the District Court stated that it would reenter the unappealed findings and conclusions without change. In these circumstances, the parties' stipulation as to the *procedure* for reentry of the unappealed second trial findings and conclusions clearly resulted in a judgment which "involve[d] a determination of questions of fact and law by the court," as expressly contemplated with respect to such procedure by the above italicized language of *International Building Co.*

(b) The Alleged Change in the "Legal Atmosphere."

The Government's alternative argument in support of its relitigation of the points established in the 1951-52 Case was that there had been a compelling change in the "legal atmosphere" respecting the depletion computation since the entry of judgment in the 1951-52 Case.

[50] E.g., *White v. Higgins,* 116 F.2d 312, 317 (1st Cir. 1940).

As its primary authority for this position it cited *Standard Lime & Cement Co. v. United States,* 329 F.2d 939 (Ct. Cl. 1964), and placed secondary reliance upon *Whitehall Cement Mfg. Co. v. United States,* 369 F.2d 468 (3d Cir. 1966).

The courts have been explicit in prescribing the type of change in the case law required to make collateral estoppel inapplicable.[51] Thus, there must be either a

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[51]For example, in *Commissioner v. Sunnen,* 333 U.S. 591 (1948), the landmark Supreme Court *Clifford-Horst* line of decisions had greatly altered the tax law of intra-family transactions between the date of the judgment claimed to have collateral estoppel effect and the second suit. In holding that such intervening Supreme Court pronouncements must override the lower court judgment in the earlier case, the Court stated:

> ". . . [A] subsequent modification of the significant facts or a change or development in the *controlling legal principles* may make that determination *obsolete or erroneous*, at least for future purposes . . . . [The principle of collateral estoppel] is not meant to create vested rights in decisions that have become obsolete or *erroneous with time,* thereby causing inequities among taxpayers . . . . [*W*]*here the situation is vitally altered* between the time of the first judgment and the second, the prior determination is not conclusive . . . . While . . . a state court decision may be considered as having changed the facts for federal tax litigation purposes, a modification or growth in *legal principles as enunciated in intervening decisions of this Court* may also effect *a significant change* in the situation." 333 U.S. 599, 600. (emphasis added)

In *Fairmont Aluminum Co.,* 22 T.C. 1377 (1954), *aff'd* 222 F.2d 633 (4th Cir. 1955), the Tax Court commented on *Sunnen* as follows:

> "The situation therein involved broad conceptual differences in legal thinking between the first proceeding and the second, and the Supreme Court approved the characterization of the series of decisions between the first and the second proceedings as '*an intervening legal development . . . which makes manifest the error of the result reached*' *in the earlier case* . . . . We think that the principle of the *Sunnen* case does not encompass so narrow a 'change' as is present here since the situation between the prior proceeding and the present one has not been 'vitally altered.'" 22 TC at 1383. (emphasis added)

(This footnote is continued on the next page)

"decisive change in the law"[52] or "an intervening legal development . . . which makes manifest the error of the result reached . . . [in the earlier case]."[53]

(i) As discussed below, instead of disagreeing with the depletion computation developed in the 1951-52 Case, the judgment in *Standard Lime* substantially supports the 1951-52 Case computation. On the major points of the treatment of cash discounts and of the costs and revenues of sacking, the *Standard Lime* judgment computation is identical with the 1951-52 Case. On the treatment of loading and shipping costs, *Standard Lime* does disagree with the 1951-52 Case computation, but resolves this point in a manner *more favorable to the taxpayer* than did the 1951-52 Case. (*Standard Lime* did not consider the other main point herein of the proper treatment of selling costs.) We cannot understand how the Government can seriously contend that *Standard Lime* changes the "legal climate," when it is so closely consistent with the 1951-52 Case and the Government itself refuses to follow the *Standard Lime* treatment of the points here pertinent.

(ii) Even if the *Standard Lime* result could somehow be viewed as inconsistent with the 1951-

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Similarly, both the Seventh and Eighth Circuits have stated that the change in "legal atmosphere" contemplated by *Sunnen* occurs "only if there has been a decisive change in the law." *Lynch v. Commissioner*, 216 F.2d 574, 580 (7th Cir. 1954); *Dr. Salsbury's Laboratories v. Russel Laboratories*, 212 F.2d 414, 416 (8th Cir. 1954). The Internal Revenue Service takes the same position in GCM 26399, 1950-2 C.B. 8, where it is stated:

> "The [Sunnen] Court held in effect that the doctrine of collateral estoppel has no application when a subsequent decision *of a court of last resort* has effected a change in the applicable legal principles." (emphasis added)

[52] *Lynch v. Commissioner,* 216 F.2d 574, 580 (7th Cir. 1954).

[53] *Commissioner v. Sunnen,* 333 U.S. 591, 603 (1948).

52 Case, it is clear that the 1951-52 Case would be the case changing the "legal climate" rather than *Standard Lime. Standard Lime* was decided one month *before* the decision of this Court in the second appeal of the 1951-52 Case and 11 months *before* the District Court's entry of final judgment in that case. If the Government really believed that *Standard Lime* changed the "legal atmosphere," it had ample opportunity to make this assertion prior to entry of final judgment in the 1951-52 Case.[54]

(iii) *Whitehall Cement* also does not change the "legal atmosphere." On the important point of the treatment of selling expenses, *Whitehall* is direct authority in support of the 1951-52 Case computation. *Whitehall* does support the Government's position respecting the treatment of the costs and revenues of sacking, but, as discussed below, this is a minority view.[55] We shall show that the main considerations on this point were not presented to the *Whitehall* court, and that the overwhelming weight of the authorities (including the *Victorville* decision of this Court) support the 1951-52 Case treatment of sacking.

As discussed *infra,* the great preponderance of the authorities continues to support the depletion computation developed in the 1951-52 Case and applied by the court below. Accordingly, we respectfully submit that the Government is completely unjustified in requiring

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[54]Contrast the effect of the Supreme Court's intervening decision in *Cannelton* on the first appeal in the 1951-52 Case. *Riddell v. California Portland Cement Co.*, 297 F.2d 345 (9th Cir. 1962).

[55]In fact, *Whitehall* is the only case which the Government has cited on this point.

California Portland and the courts to submit to a relitigation for 1953-59 of the same depletion computation which was so laboriously determined in the 1951-52 Case.

(c) The Effect of the 1951-52 Case on the Depletion Computation of the Arizona Company.

The Government contends that the 1951-52 Case has no bearing on the Arizona Company's depletion computation. We believe this is clear error.

During the period of the Arizona Company's operations concerned herein (1953-57), that company was at all times a wholly owned subsidiary of California Portland.[56] Effective August 31, 1961, it was merged into California Portland.[57] The District Court made the following finding with respect to the Arizona Company (referred to therein as "Taxpayer"):

> "17. During the taxable years ended April 30, 1953, April 30, 1954, April 30, 1955, April 30, 1956, and April 30, 1957, the relevant facts and circumstances pertaining to the Taxpayer's (i) production of cement clinker, bulk cement, sacked cement and the marketing thereof, (ii) cash discount practices, and (iii) selling expenses, were in substance identical with the relevant facts and circumstances pertaining to such items of the plaintiff [California Portland] during the earlier taxable years ended April 30, 1951 and April 30, 1952, as found by this Court in the action captioned *California Portland Cement Co. vs. R. A.*

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[56] No. 22397, I-R. 120.

[57] *Ibid.*

> *Riddell, District Director of Internal Revenue, Los Angeles District* (No. 135-58 WM, Civil), decided on February 16, 1965. At all times relevant hereto, the Taxpayer has been and now is in privity with the plaintiff."[58]

This Finding is clearly supported by the evidence.[59]

The identical circumstances here concerned were before the District Court in *Monolith Portland Cement Co. v. Riddell,* and *Monolith Portland Midwest Co. v. Riddell.*[60] In *Monolith,* the taxpayer was a cement producer with respect to which the District Court had previously determined the method of computing its percentage depletion for the taxable year 1951.[61] In a second action involving the taxable year 1952, the Government sought to reopen the previously established method of computing the taxpayer's depletion. The District Court held that collateral estoppel applied, as follows:

> "The defendant asserts that issues of fact do exist with regard to the character or classification of plaintiff's limestone, whether plaintiff's processes were ordinary and those usually applied, and what was plaintiff's commercially marketable mineral product in 1952.
>
> "In the Court's view, all of these issues were litigated and decided adversely to this defendant's privy, the United States of America, in the 1951

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[58]*Id.* at 125-26.

[59]E.g., *id.* at 80-81, 120.

[60]Unofficially reported at 60-1 USTC para. 9187 and 62-2 USTC para. 9750, respectively.

[61]168 F. Supp. 692; *aff'd and remanded,* 269 F.2d 629 (9th Cir. 1959).

> case . . . [citations omitted]. Hence such issues are not now available to the defendant here, under the doctrine of res judicata and collateral estoppel. *The Government may not force the plaintiff to relitigate each tax year the question of the depletion statute's applicability to plaintiff's status, where the undisputed and admitted facts show that such status has remained unchanged."* (emphasis added)

The same result was reached by the District Court in the *Midwest* case, where Monolith's wholly owned subsidiary, Midwest, was held in privity with Monolith and entitled to the collateral estoppel effect of the 1951 litigation involving Monolith.[62]

Based upon the foregoing, we believe that the 1951-52 Case collaterally estops the Government from attacking the Arizona Company's depletion computation, as well as that of California Portland. Even if collateral estoppel were held inapplicable to the Arizona Company, however, the 1951-52 Case should still control that company's depletion computation as a matter of *stare decisis,* since the facts in the two cases are in substance identical.

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[62] Subsequent to the District Court's holdings in *Monolith* and *Midwest* and while such decisions were on appeal to this Court, *United States v. Cannelton Sewer Pipe Co.,* 364 U.S. 76 (1960), was decided by the United States Supreme Court. This event, which shifted the depletion cut-off from the end product to an intermediate processing stage, constituted a true change in the "legal atmosphere," and both *Monolith* and *Midwest* were reversed solely on the basis of *Cannelton.* As previously discussed, no such change in the "legal atmosphere" has occurred in the present case, and therefore the District Court's *Monolith* and *Midwest* decisions are direct authority for applying collateral estopped here.

II.

THE RELIANCE OF THE DISTRICT COURT UPON THE RESULT REACHED IN THE 1951-52 CASE IS SUPPORTED BY THE MERITS AS WELL AS BY COLLATERAL ESTOPPEL.

A. Introduction.

As previously discussed, the facts in the instant case are identical in all material particulars with those in the 1951-52 Case.[63] This portion of our brief will examine the merits of the depletion computation determined in the 1951-52 Case, and shall demonstrate that the District Court's adherence to that computation was correct and should be affirmed.

A miner of calcium carbonates such as California Portland[64] is entitled to a percentage depletion deduction at the rate of 15%.[65] The sole substantive issue in this case is the proper method of computing the amount against which such 15% rate is to be applied (herein called the "depletion base").

The purpose of the depletion deduction is to compensate for the exhaustion of a taxpayer's mineral deposit, and to provide an inducement for mineral exploration and development.[66] The statute has been drafted to

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[63]Nn. 13 & 15, *supra.*

[64]To simplify discussion of the merits, reference shall be limited to the case of California Portland, since the material facts and the depletion computation pertaining to California Portland and the Arizona Company are identical. The Government agrees with this approach. Gov't. Op. Tr. Br. 3, n. 1.

[65]Int. Rev. Code of 1954, § 613(b)(7). (See also n. 11, *supra.*) Such 15% rate is subject to a limit of "50% of the taxpayer's taxable income from the property" (Section 613(a)), but in this case the 15% depletion allowances are significantly less than the 50% limit.

[66]*United States v. Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960) [hereinafter cited as *"Cannelton"*].

permit the deduction not only with respect to the value of the mineral in the ground, but also with respect to certain processes necessary to extract the mineral and to place it in a condition so it may be sold ("mining processes").[67] Beyond this point, however, the right to depletion ceases, and processes applied thereafter to change the mineral into a different product ("manufacturing processes") are not depletable.[68]

The simplest case is that of a nonintegrated miner, selling raw mineral after extraction but prior to the application of any process considered as manufacturing. In such case the depletion base is the miner's entire gross income from the sale of the raw mineral product.[69]

Difficulty is encountered when the taxpayer is both a miner and a manufacturer, extracting the raw mineral and then processing it into what the law considers to be a manufactured product. If the mineral processed by the miner-manufacturer is the same as that extracted and sold in commercial quantities by nonintegrated miners in his market area, the miner-manufacturer is required to use as his depletion base the local price of the raw mineral.[70] Where, as in the present case, the miner-manufacturer processes mineral which is not sold by nonintegrated miners, to determine the depletion base it is necessary to construct an artificial price at a point where the law presumes a nonintegrated miner would sell, if in fact there had been any demand for the mineral at such stage of processing.[71]

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[67] Section 613(c); *Cannelton.*

[68] *Cannelton.*

[69] Section 613(c); INT. REV. CODE OF 1939, Reg. 118, § 39.23-(m)-1(e) [hereinafter referred to as "Regulation 118"]; *Cannelton.*

[70] *Cannelton.*

[71] Subsection (3) of Regulation 118.

With respect to producers of cement, Congress has enacted an elective[72] provision that such point of presumed sale at which "mining" ends and "manufacturing" begins is the point in the cement production process where the raw mix is ready for introduction into the rotary kilns (herein called "the kiln feed cutoff").[73] California Portland made a timely election to be governed by this provision[74] and, accordingly, must compute its depletion base at the price at which nonintegrated miners would sell kiln feed. In fact, however, no one sells kiln feed,[75] and therefore it is necessary to take the price of the first commercially[76] marketable product of the cement making process, and work back from that price to construct a theoretical price for kiln feed. Such construction of a theoretical price for kiln feed from the price of the subsequent product is accomplished by the proportionate costs and

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[72]The provision is elective with respect to taxable years commencing prior to January 1, 1961. Thereafter it is mandatory. P.L. 86-564 (74 Stat. 290); P.L. 86-781 (74 Stat. 1017).

[73]Section 613(c)(4)(F); P.L. 86-564 (74 Stat. 290); P.L. 86-781 (74 Stat. 1017).

[74]No. 22398, I-R. 151; No. 22397, I-R. 103-04.

[75]Pltf. Ex. 20-B, 186-87. Pursuant to stipulation, the affidavits of certain witnesses and deposition testimony thereon were treated as direct testimony at the trial. Tr. 56; No. 22398, I-R. 130-32; No. 22397, I-R. 61-63.

[76]The Government claims that the District Court was confused in relying on the concept of a "commercially" marketable product. App. Br. 29-32. Subsection (3) of Regulation 118 does speak of the "first marketable product." In subsection (2), however, it makes clear that this reference is to a "commercially" marketable product. The point was important below, because the Government then contended that California Portland's *de minimus* sales of cement clinker established its "first marketable product" and the starting point for its depletion computation. This was clearly erroneous because cement clinker is not a "commercially" marketable product (see, e.g., Pltf. Op. Tr. Br. 72-82), and the Government now admits that California Portland has no "first marketable product" prior to finished cement. App. Br. 34.

profits computation specified in subparagraph (3) of Section 39.23(m)-1(e) of Regulation 118 under the Internal Revenue Code of 1939 (which provision is hereinafter referred to as "Regulation 118").[77]

The computation requires that the costs of producing the first commercially marketable product of the cement making operation be allocated to either mining processes or manufacturing processes. After such allocation, the depletion base constructive kiln feed price is that percentage of the price of the first commercially marketable product which the costs attributable to mining processes bear to the total costs attributable to the mining and manufacturing processes resulting in the first commercially marketable product.[78]

In the present case the areas of disagreement are (i) the selection of the first commercially marketable product to be used as the starting point for constructing the kiln feed price and (ii) the allocation of specific costs to either mining or manufacturing.

The selection of the first commercially marketable product makes a substantial difference in the constructive kiln feed price, because the marketable product sales price is the amount against which the ratio developed by Regulation 118 is applied. Thus, if the Regulation 118 ratio was 30%, the constructive kiln feed price would change substantially depending on whether

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[77]Regulation 118 was made applicable to 1954 Code years by T.D. 6091, 1954-2 C.B. 47.

[78]The above is intended merely to summarize the pertinent computational provision. These matters are developed in detail, *infra.*

the first commercially marketable product had a price of $100 or $150. In similar manner, the characterization of costs as attributable to either mining or manufacturing is also very important, because a determination that a cost is a "mining cost" increases the Regulation 118 ratio (and the constructive kiln feed price) while the converse is true if it is determined that such cost is attributable to manufacturing.

The specific questions on the merits of the depletion computation developed in the 1951-52 Case and applied by the District Court below are as follows:

(a) Whether California Portland's first commercially marketable product is bulk cement or sacked cement.

(b) The proper treatment in the depletion computation of selling expenses.

(c) The treatment of cash discounts.

(d) The treatment of the costs of handling certain pre-kiln "additives."

In addition to the above matters, there is a further question of the propriety of California Portland's alternative treatment of loading and shipping costs. California Portland seeks to raise this alternative contention only if this Court does not adhere to the depletion computation established in the 1951-52 Case and by the District Court.

Since the income from California Portland's first commercially marketable product is the starting point for the Regulation 118 computation, item (a) above shall be discussed first.

B. California Portland's First Commercially Marketable Product.

1. The Proper Starting Point for the Regulation 118 Computation Is the Sale of Cement in Bulk. Sacked Cement Is Not the First Marketable Product and Should Be Excluded From the Computation.

Regulation 118 provides in pertinent part as follows:

> "(3) If the taxpayer sells the crude mineral product . . . in the immediate vicinity of the mine, 'gross income from the property' means the amount for which such product was sold, but, if the product is . . . processed (other than by the ordinary treatment processes . . .) before sale, 'gross income from the property' means the representative market or field price . . . of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes. . . . *If there is no such reppresentative market or field price . . . then there shall be used in lieu thereof the representative market . . . price of the first marketable product resulting from any process or processes . . . minus the costs and proportionate profits attributable to . . . the processes beyond the ordinary treatment processes."* (emphasis added)

In the present case, the statute provides that the "crude mineral product" which establishes California Portland's depletion base is the kiln feed.[79] Neither California Portland nor anyone else in the industry sells kiln feed, however.[80] Accordingly, the only provision of Regulation 118 which applies here is the portion italicized above. Said provision states that the

[79] Int. Rev. Code of 1954, § 613(c).
[80] Pltf. Ex. 20-A 186-87; App. Br. 19.

starting point for the depletion computation is "the representative market . . . price of the first marketable product resulting from any process or processes. . . ."[81]

The Government contends: "The first 'marketable product' was finished cement; the finished cement was sold both in bulk and in bags."[82] This assertion that the *first* marketable product was *both* bulk and sacked cement has no basis in the record, and the Government does not even attempt a record reference. The District Court found as a fact that the first marketable product obtained from California Portland's calcium carbonate rock was bulk (as opposed to sacked) cement.[83] This finding is clearly supported by the evidence.[84]

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[81]As discussed in n. 76, the "first marketable product" must be "commercially" marketable. There is no issue whether bulk cement can be sold in commercial quantities, however, and the only question is which of two marketable products is first—bulk or sacked cement.

[82]App. Br. 34.

[83]No. 22398, I-R. 184-85; No. 22397, I-R. 124-25.

[84]More than 75% of California Portland's cement was sold in bulk, and the sacking of the remaining portion occurred after the bulk cement had been produced and was ready for sale. No. 22398, I-R. 105-10; No. 22397, I-R. 73; Pltf. Ex. 20-A 189-90. The Government's witness David Caldwell testified as follows:

> "Q. Wouldn't you describe the bagging of cement as an operation which occurred subsequent to the production of bulk cement?
>
> A. Yes, sir. There is no question about that." Pltf. Ex. 19, 118.

In response to a hypothetical question involving a taxpayer who sold one-half of his output as bulk cement and one-half as ready-mix concete, Mr. Caldwell further testified that the Regulation 118 ratio respecting the total output would have to be applied against the bulk cement price. *Id.* at 121.

Defendant's principal witness Arnold Lintz testified as follows:

> "Q. Well, where cement is sold beyond the bulk cement stage, what has your position been as to the first marketable product?

(This footnote is continued on the next page)

In *Riddell v. Victorville Lime Rock Co.,* 292 F.2d 427 (9th Cir. 1961), the taxpayer quarried and ground high grade limestone, which it sold to the paint industry for use in paint manufacture and to builders for roofing granules, stucco, and plaster. The taxpayer's production was sold both in bulk and in bags. This Court held as follows:

> ". . . [T]he district court erred in including in appellee's depletion base income attributable to bags and bagging. . . . *Bags and bagging are not required to obtain the commercially marketable mineral product.* Income attributable to bags and bagging should have been excluded. . . ." 292 F.2d at 436. (emphasis added)

At the first trial in the 1951-52 Case, the District Court held that, as to that portion of California Portland's production sold in sacks, sacked cement was the first commercially marketable product.[85] On remand after the *Cannelton* decision and California Portland's kiln feed election, the District Court followed *Victorville* and treated bulk cement as California Portland's first marketable product, excluding both the costs and revenues of sacking from the depletion computation.[86] Numerous authorities clearly establish that the treatment of sacking in *Victorville* and the 1951-52 Case was correct.

"A. It is still cement. The bags have nothing to do with the first marketable product.

"Q. What is the first marketable product of California Portland Cement on the basis of which your computations were made?

"A. Well, it includes bagged cement. This is true." *Id.* at 14.

[85]No. 16438, I-R. 138-39, 144 (Findings 13 and 26).

[86]No. 18506, R. 17 (Finding 28). As previously mentioned, the Government did not appeal this determination in the 1951-52 Case. No. 18506, R. 171.

In *United Salt Corporation*, 40 T.C. 359 (1963), *aff'd per curiam*, 339 F.2d 215 (5th Cir., 1965), the taxpayer sold about 30% of its salt in bulk and nearly 60% in sacks. In holding that the reference point for the depletion computation was the bulk product, the court stated:[87]

> "Petitioner's contention that it is entitled to determine the 'gross income from the property' on the basis of its gross income from the sale of *all* its salt products f.o.b. plant loaded for shipment . . . is untenable in view of the principles of the *Cannelton* case and cases subsequent to it. Clearly, the costs of sacking and sewing are not includable in the depletion base. . . .
>
> "We find that petitioner's depletion base is the gross income it would have received if it had sold all of its salt in the years before us as bulk salt." (original emphasis)

Similarly, in *Standard Realization Co.*, 289 F.2d 247 (7th Cir. 1961), the taxpayer mined quartzite and processed it to varying degrees of fineness. More than 60% of its product was sold in bulk. The court held that the depletion computation must be made on the basis of what the taxpayer would have received if all of its product had been sold in bulk, without consideration of sacking or other subsequent activities.

In *North Carolina Granite Corp.*, 43 TC 149 (1964), the taxpayer quarried granite which it crushed and ground and then sold for use as poultry grit or road material. The court held as follows:

> "After the screening process, the crushed granite destined for sale as poultry grit is sent through

[87]40 TC at 368.

> spouts into the bagging room. We hold, as to this portion of petitioner's crushed granite, that 'mining' ceases when the crushed granite reaches the bagging room, and that petitioner's 'gross income from the property' is the amount it would have received if it had sold the mineral in bulk at this stage [citing *Cannelton, Standard Realization,* and *United Salt*]." 43 TC at 157.

As discussed below,[88] the Government's principal authority in this case, *Standard Lime,* is also in precise accord with the court below on the treatment of sacked cement in the depletion computation.

The next section of this brief shall show that the whole purpose of the Regulation 118 computation is to work back from the price of a product which is actually sold and construct a price or value of the kiln feed, which is not sold. Obviously the price or value of the kiln feed for a particular taxpayer should be a uniform amount, since the kiln feed is a uniform, fungible product. Therefore, a computation which, as suggested by the Government, works back from two or more products of a single taxpayer and establishes different constructive prices for its kiln feed, violates the clear purpose of the Regulation as well as its express "first marketable product" requirement. This may be illustrated by the following example:

Assume a lot of cement sold for $1300, total costs and allocable expenses of mining and manufacturing were $250 and $750 respectively, profit was $100, and

[88]Pp. 60-61, *infra*.

expenses of sacks and sacking and sack premium were $200. Gross income from mining of the bulk cement and sacked cement would be calculated as follows:

		Bulk	Sacked
1.	Sales proceeds of bulk cement	$1100	$1100
2.	Sack premium	....	200
3.	Total sales proceeds	$1100	$1300
4.	Production Costs and Expenses:		
5.	Mining	$ 250	$ 250
6.	Manufacturing	750	750
7.	Sacks and Sacking	....	200
8.	Total costs and expenses	$1000	$1200
9.	Net Profit	$ 100	$ 100
10.	Regulation 118 ratio (Item 5 over item 8)	250/1000	250/1200
11.	Gross income from mining—constructive price of kiln feed (Item 10 x item 3)	$ 275	$ 271

The foregoing makes it clear that the only way to reach the required uniform depletion base of the value of the fungible product of kiln feed is to work back from the uniform price of the first marketable product. The Government's contention of working back from products other than bulk cement distorts the calculation and violates (i) the purpose of the calculation, (ii) the express language of Regulation 118, and (iii) the pertinent judicial authorities, including the *Victorville* decision of this Court.[89]

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[89]The only case which the Government has cited in its favor on the first marketable product question is *Whitehall Cement Mfg. Co. v. United States,* 369 F.2d 468 (3d Cir. 1967). We do not believe the Court was correctly informed on this point, and have discussed the case in a separate section at pp. 61-62, *infra.*

C. The Allocation of California Portland's Costs to Its Mining and Manufacturing Activities.

1. Introduction.

In the preceding section we established that bulk cement is California Portland's first commercially marketable product and the starting point for the Regulation 118 computation. The next question is the manner in which that computation works back from the sales income at said starting point to establish a constructive price or value of California Portland's calcium carbonate rock at the kiln feed cut-off point.

Subsection 613(c) of the Internal Revenue Code of 1954 provides that the depletion base shall be the taxpayer's "gross income from mining." Said subsection then defines "mining" as follows:

> ". . . (2) MINING.—The term 'mining' includes not merely the extraction of the ores or minerals from the ground but also the treatment processes considered as mining described in paragraph (4) (and the treatment processes necessary or incidental thereto). . . .
>
> "(4) TREATMENT PROCESSES CONSIDERED AS MINING.—The following treatment processes where applied by the mine owner or operator shall be considered as mining. . . .
>
> > (F) in the case of calcium carbonates and other minerals when used in making cement—*all processes* (other than pre-heating of the kiln feed) *applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process; . . .*" (emphasis added)

This statutory language makes it clear that the "mining" activities of an integrated producer of cement

stop at the kiln feed stage, and that the "gross income from mining" at that point is to be determined by allocation of costs and profits to pre-kiln feed treatment *processes* and to subsequent treatment *processes*. The same principle is established by Regulation 118:

> ". . . If there is no such representative market or field price . . ., then there shall be used in lieu thereof *the representative market . . . price of the first marketable product* resulting from any process or processes . . . *minus the costs and proportionate profits attributable to . . . the processes beyond the ordinary treatment processes*." (emphasis added)

California Portland's first marketable product is bulk cement. Subsection 613(c)(4)(F) establishes that the "ordinary treatment processes" referred to in Regulation 118 terminate at the kiln feed stage. Accordingly, the Regulation 118 computation expressly requires that California Portland's gross income from sales of bulk cement be reduced by only the costs and proportionate profits attributable to the *processes* beyond the kiln feed cut off point, and that all of the remainder be treated as California Portland's depletion base "gross income from mining." Only a simple matter of subtraction is involved.

The Regulation 118 computation has been expressed in other ways by several courts. For example, in the principal case relied on by the Government, *Standard Lime & Cement Co. v. United States*, 329 F.2d 939 (Ct. Cl. 1964), the court anaylzed the computation as follows:[90]

> (i) The statute divides an integrated cement producer's operation into processes up to kiln feed

[90] 329 F.2d at 944-45.

and post-kiln feed processes. The first step in the computation is to determine the direct costs which are associated with each part of the total flow of processes.

(ii) The second step is to determine the indirect costs which are incurred for the benefit of the entire operation. These are allocated to pre and post kiln feed processes in the proportion that the direct process costs on each side of the cut-off point bear to the total direct process costs.

(iii) The third step is to take the total profit from the cement producing operation and reduce it by the profit attributable to indirect costs which do not benefit the entire operation. The remaining or "net" profit is allocated to pre and post kiln feed processes in the proportion that the direct process costs on each side of the cut-off point bear to the total direct process costs.

(iv) The taxpayer's "gross income from mining" is the sum of the costs and profits allocated to pre-kiln feed processes pursuant to the above three steps.

A simplified statement of the Regulation 118 computation has also been made by the *Whitehall*[91] court and this Court.[92] As stated by this Court, the formula may be expressed as:[93]

$$\frac{\text{“mining” costs}}{\text{total costs of product sold}} \times \begin{array}{c}\text{sale price of}\\ \text{product sold}\end{array} = \begin{array}{c}\text{gross income}\\ \text{from mining}\end{array}$$

The Government's case is based on its interpretation of this simplified statement of the computation. Brief-

[91] *Whitchall Cement Mfg. Co. v. United States,* 369 F.2d 468 (3d Cir. 1966).

[92] See *Riddell v. California Portland Cement Co.,* 330 F.2d 16 (9th Cir. 1964).

[93] 330 F.2d at 17.

ly, the Government's argument is (i) all costs must be expressly included in the depletion computation,[94] (ii) "no part of an integrated producer's costs (other than direct mining process costs) may be allocated to mining unless there is a discernible, demonstrable benefit to mining and the crude mineral product thereof,"[95] and (iii) any cost not "discernably" and "demonstrably" benefiting mining must automatically be placed in the denominator of the simplified computation.[96]

We submit that this is an erroneous interpretation of a formula which itself was intended merely to summarize and simplify the Regulation 118 computation.

(a) The Government's statement that all costs must be expressly included in the simplified depletion computation is misleading and, with respect to certain costs, incorrect. As stated in *Standard Lime*,[97] allocable indirect costs are allocated in the computation on the basis of direct process costs. Accordingly, if direct pre-kiln feed process costs are $10 and direct post-kiln feed process costs are $20, the pre-kiln feed to total process cost ratio is 1:3. If allocable indirect costs are then allocated to both sides of the cut-off point in proportion to the direct process costs, the depletion ratio remains 1:3. Obviously, therefore, it was not error for the District Court to hold that allocable indirect costs could either be included or excluded from the ratio computation[98]—the result remains the same either way. In addition, the preceding analysis has shown that incremental costs and revenues attributable

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[94]App. Br. 22.
[95]*Id.* at 25.
[96]*Id.* at 23.
[97]329 F.2d at 945.
[98]See, e.g., No. 22398, I-R. 185 (Finding 22).

to products after the first marketable product are to be excluded from the depletion computation.[99]

(b) The Government's argument that all indirect costs are automatically included in the denominator of the simplified computation unless they "discernably" and "demonstrably" benefit mining has even less merit.

(i) The express language of Regulation 118 establishes a subtraction formula. Costs and profits are allocated to post-kiln feed *processes;* this amount is deducted from the price of the first marketable product, and the entire remainder constitutes "gross income from mining." Using the Government's argument in relation to the express language of Regulation 118, therefore, if a cost could not establish a "discernable, demonstrable benefit" to post kiln feed treatment processes, it must *remain* as a mining cost.[100]

(ii) The *Standard Lime* quotation[101] relied on by the Government to support its alleged "non-mining" presumption is out of context. As noted above, the court had previously made clear that the allocation inquiry was whether an indirect cost benefited the *entire* extraction-production operation.[102] In addition, the *Standard Lime* court

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[99]Pp. 30-35, *supra.* See also the *Standard Lime* treatment of sacking at 329 F.2d 948-49 and Pltf. Ex.1.

[100]The correct position is that there is no presumption of allocation to either side of the kiln feed cut-off point. Allocation must be determined by reference to (i) the nature of the cost, (ii) the particulars of the industry concerned, and (iii) the purpose of the depletion computation. See pp. 42-45, *infra.*

[101]App. Br. 24-25.

[102]". . . [T]he total indirect costs which are incurred for the benefit of the *entire* operation are determined. These indirect costs are allocated to the first part of taxpayer's operation in the proportion as this part's direct costs bear to the aggregate direct costs." 329 F.2d at 945. (original emphasis)

specifically rejected the Government's argument that the denominator of the computation formula was a catch-all for all "non-mining" costs and, instead, held that if a cost which was not directly attributable to the flow of treatment processes did not benefit the entire mining-manufacturing operation, then such cost and the profits attributable thereto should be excluded from the computation.[103]

(iii) The statute and Regulation 118 speak of a flow of *process* costs. The context of the statute shows that the reference to "processes" means "treatment processes."[104] The leading judicial authority, *Cannelton,* states that the purpose of the depletion computation is that "the miner-manufacturer . . . [shall not] enjoy, in addition to a depletion allowance on his minerals, a similar allowance on his *manufacturing costs. . . .*"[105] Similarly, the court in *United States v. Henderson Clay Products,* 324 F.2d 7 (5th Cir. 1963), described the Regulation 118 computation as "a means of disintegrating an integrated company back into separate mining and processing entities."[106]

(iv) For the above reasons, it appears that much of the confusion caused by the Government's interpretation of the simplified statement of the Regulation 118 formula could be eliminated if that formula were stated as follows:

$$\frac{\text{Mining costs}}{\text{Total mining and manufacturing costs}} \times \begin{array}{l}\text{Gross income from}\\ \text{first marketable}\\ \text{product}\end{array} = \begin{array}{l}\text{Gross income}\\ \text{from mining}\end{array}$$

[103] 329 F.2d at 945, 948 n. 19; Pltf. Ex. 1.

[104] See n. 127. *infra.*

[105] 364 U.S. at 88.

[106] 324 F.2d at 15.

This would place the emphasis in allocating indirect costs where it belongs, i.e., on the disintegration of an integrated miner-manufacturer into separate mining and manufacturing entities.

2. The Purpose of the Regulation 118 Computation.

By their very nature, indirect costs are often difficult to allocate to a particular process. It would appear evident that any such allocation in the depletion computation should be made by express reference to the purpose of that computation.

The leading case with respect to the depletion base computation is *United States v. Cannelton Sewer Pipe Co.,* 364 U.S. 76 (1960). There, the taxpayer extracted fire clay and shale from an underground mine, and then manufactured the minerals into vitrified sewer pipe and related products. The taxpayer contended that its depletion base should be the sales revenue from its manufactured end products. The Government argued that the depletion base should be the price at which nonintegrated miners sold the same crude mineral as that extracted by the taxpayer. In resolving this question, the Supreme Court made a careful analysis of the intent of the depletion allowance, as follows:

> "We have concluded that, under the mandate of the statute, respondent's 'gross income from mining' under the findings here is *the value* of its raw fire clay and shale, after the application of the ordinary treatment processes normally applied by nonintegrated miners engaged in the recovery of those minerals. . . .[107]
>
> "The Shepherd Report . . . [recognized] that *processing beyond this point should not be included* in calculating 'gross income from the property'.

[107] 364 U.S. at 78.

. . . [T]he report also proposed that the depreciation [sic] base 'in the case of all other metals, coal and oil and gas,' [should be] *the competitive market receipts, or its equivalent, received from the sale of the crude products*, or concentrates on an f.o.b. mine, mill, or well basis. . . .[108]

"From this legislative history, we conclude that Congress intended to grant miners a depletion allowance based on *the constructive income from the raw mineral product,* if marketable in that form, and not on the value of the finished articles. . . .[109]

". . . [R]espondent says that the processes it uses are the ordinary ones applied in the industry. As to the miner-manufacturer, that is true. But they are not the 'ordinary' normal ones applied by *the nonintegrated miner. It was he whom Congress made the object of the allowance.* The fabrication processes used by respondent in manufacturing sewer pipe would not be employed by the run-of-the-mill miner—only an integrated miner-manufacturer would have occasion to use them. . . .[110]

"We believe that the Congress intended integrated mining-manufacturing operations to be treated as if the operator were selling the mineral mined to himself for fabrication. *It would, of course, be permissible for such an operator to calculate his 'gross income from mining' at the point where 'ordinary' miners—not integrated—disposed of their product. . . .*"[111] (emphasis added)

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[108]*Id.* at 82-83.
[109]*Id.* at 86.
[110]*Id.* at 87-88.
[111]*Id.* at 89.

The Supreme Court's reasoning makes it clear that the depletion computation of an integrated miner-manufacturer should produce the same depletion deduction as that of a nonintegrated miner, whose depletion base is the gross revenue from sales of the crude mineral product (as beneficiated by allowable processing treated as "mining").[112]

The same purpose was emphasized by the Treasury representative, testifying before the House Ways and Means Committee with respect to the Treasury proposal which resulted in enactment of the kiln feed cut-off point for cement producers:[113]

> "MR. LINDSAY. Let me say this generally about cutting back, taking a proportionate amount of the profit from the finished product.
>
> "Where there is a market for the raw mineral at the stage at which percentage depletion is going to be allowed, that probably is a fair measure of the proportionate profit attributable to that raw mineral, proportionate profit from the sale of the finished product.
>
> "Now, you could work back to that on a formula and it may be that you come out with the same

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[112]The Government makes the surprising statement that "the *Cannelton* and *Monolith* decisions had nothing whatever to do with how an integrated producer's constructive income from mining should be computed." App. Br. 30. Both of said cases involved integrated producers, and in *Cannelton* the court specifically stated that the depletion allowance is to be based on "the constructive income from the raw mineral product . . . ." 364 U.S. at 86. Clearly the depletion computation's purpose of giving an integrated producer the same depletion base as that of a nonintegrated miner does not change whether the Regulation 118 reference is to a representative market or field price based on actual mineral sales or to a constructive market price derived by working back from sales of a subsequent product.

[113]*Hearings Before the House Committee on Ways and Means on Mineral Treatment Processes for Percentage Depletion Purposes,* 86th Cong., 1st Sess. (March 5, 1959).

result as you would have if you looked at the quoted price for that raw material. *Ideally the two systems would come out with the same result.*

"I do not think they always will. There will be minor differences. . . .

"If a taxpayer does not sell the crude mineral, but processes it beyond the mining stage, the regulations provide that the market price of the gross income product must be determined by the use of appropriate methods *with the objective of determining as accurately as practicable the price at which such gross income product would be sold if such commercial sales existed.*"[114] (emphasis added)

3. California Portland's Selling Expenses Clearly Benefit and Are Attributable to Its Entire Mining-Manufacturing Operation.

During the years concerned, California Portland incurred certain selling expenses with respect to the products of its integrated mining and manufacturing processes. These consisted primarily of expenses of membership in various industry trade associations, and the salaries and other expenses of salesmen.[115] The District Court found that these expenses did not represent the cost of any process applied to California Portland's calcium carbonate rock, and that such expenses were necessary and of benefit to both California Portland's mineral product and to its manufactured prod-

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[114] *Id.* at 46-47, 49.

[115] No. 22398, I-R. 185 (Finding 22).

uct.[116] This finding is completely supported by the evidence.[117]

The Government makes no reference to the record in opposition to the District Court's finding.[118] Instead, it makes a theoretical argument which illustrates the fallacy of its position that there is a presumption respecting the allocation of indirect costs in the depletion computation. The Government cannot find a close relation of selling expenses to mining processes, and concludes from this that such expenses must therefore be automatically allocated to manufacturing. In fact, however, as found by the District Court, selling expenses "did not represent the cost of *any process* applied to plaintiff's calcium carbonate rock."[119] (emphasis added) Applying the Government's logic to the express language of Regulation 118, selling expenses do not represent manufacturing processes, and since only the costs of such processes (and the profits attributable thereto) are subtracted from the first marketable product price,[120] *all* selling expenses should be included in the depletion base.

The District Court's finding that selling expenses are necessary and of benefit to both the mineral product and the manufactured product is supported by common sense as well as by the evidence. Since the objective of the depletion computation is to construct the price at which a hypothetical nonintegrated producer would sell kiln feed, and since the method of construt-

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[116]*Ibid.*

[117]Pltf. Ex. 19, 116-17; Pltf. Ex. 20 B-C, 240-41, 358, 360, 370-72.

[118]See App. Br. 36-39.

[119]N. 115, *supra*.

[120]See quotation of the Regulation and discussion at pp. 37, 40, *supra*.

ing such price is to develop the costs which such non-integrated producer would incur, it is plain that some selling expenses should be included in the depletion base.[121]

The Government admits in this case that California Portland's general and administrative expenses benefit both the mineral product and the manufactured product, and may be allocated to each such product in the ratio of direct mining process costs to total direct mining and manufacturing process costs.[122] In contending that selling expenses are exclusively manufacturing costs, however, the Government ignores the close analogy of such expenses to general and administrative expenses, its own previous publications, and the pertinent authorities.

Although an integrated miner-manufacturer is entitled to a percentage depletion allowance on the *gross* income from its mineral product, that allowance is limited by 50% of the taxable income from such product.[123] In determining taxable income, all costs and expenses which generate the "gross income from mining" must be deducted from such gross income. In the case of an integrated miner-manufacturer, therefore, the "mining" cost allocation serves two purposes: it provides the basis by which "gross income from mining" is determined, and it also provides the costs which are deducted from such gross income to yield taxable income from "mining." In its own Regulations on the computation of taxable income from mining for percentage depletion purposes, the Government expressly requires that an integrated miner-manufacturer allocate

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[121]An apt discussion of this conclusion is made by the District Court in *Whitehall*, quoted at pp. 51-52, *infra*.

[122]See Def. Ex. A (e.g., pp. 1-2 of ex. A thereto).

[123]INT. REV. CODE of 1954, § 613(a).

a pro-rata portion of his first marketable product selling expenses to "mining costs," as follows:

> "The term 'taxable income from the property' . . . as used in section 613 . . . means 'gross income from the property' as defined in section 613(c) . . . less *allowable deductions . . . attributable to ordinary treatment processes. . . .* [i.e., "mining"] *These deductions include* administrative and financial overhead, operating expenses, *selling expenses,* depreciation, taxes, losses sustained, etc. . . . Expenditures which may be attributable to both the mineral property upon which depletion is claimed and other activities shall be fairly apportioned."[124] (emphasis added)

In *Island Creek Coal Co. v. Commissioner,* 382 F.2d 35 (4th Cir. 1967), the court discussed the 50% of taxable income limitation as follows:

> "The statute does not explicitly define the term 'taxable income from the property.' There was no necessity of it, for the definition of 'gross income from property' in terms of 'mining' and the included treatment processes make it perfectly clear that 'taxable income from the property' means taxable income from mining and the included treatment processes. *Taxable income from mining is computed by deducting from gross income from mining all of the mining expenses incurred in the production of that income.* An expense incurred to produce income which is not income from mining, is not an expense of mining."[125] (emphasis added)

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[124] Reg. § 1.613-4.
[125] 382 F.2d at 37.

Since the same costs which are included in "gross income from mining" are deducted in determining "taxable income from mining," it is obvious that if selling expenses are deductible in determining such taxable income, they must already have been part of "gross income from mining" to begin with. This has also been recognized by the Government in an express ruling that a nonintegrated producer may include selling expenses in his depletion base. Thus, in *Rev. Rul.* 60-98, 1960-1 C.B. 252, the summary of the Ruling states:

> "Where a mine operator sells his product through a *del credere* sales agent, the full sales price, unreduced by the sales commission, is the 'gross income from the property' for purposes of percentage depletion under Section 613(c) of the Internal Revenue Code of 1954."

Apart from a single trial court decision in Alabama,[126] the Government has not cited any case which upholds its present position that selling expenses are exclusively manufacturing costs.[127] The Government's theory appears to have arisen for the first time in

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[126] *United States Pipe & Foundry Co. v. Patterson,* 203 F. Supp. 335 (N.D. Ala. 1962).

[127] The Government does seek support (App. Br. 38-39) from the following quotation from *Standard Lime:*

> "The language of subparagraph (F) of subsection 613(c) (4) . . . specifically includes all processes up to kiln feed, 'but not including any subsequent processes.' We interpret this as excluding any subsequent manufacturing or *marketing processes.*" 329 F.2d at 946. (emphasis added)

We believe that the court's reference to "marketing processes" cannot be extended to selling expenses for the following reasons:

(i) *Standard Lime* did not involve selling expenses (329 F.2d at 942), and the above *dictum* was made in response to the taxpayer's contention that the issue was merely one of proper accounting treatment. (329 F.2d at 945-46).

(This footnote is continued on the next page)

1964 in *North Carolina Granite Corp., supra.* In rejecting this departure from the Government's published requirements and position, the court stated as follows:[128]

> "It is apparent that . . . [the Government's] argument rests in large measure upon its conclusions that the high price received by petitioner for poultry grit is chiefly attributable to *'nonmining processing'* in the form of advertising, goodwill, trademark, and *selling expenditures,* and that, absent such 'processing,' bulk poultry grit would command a price no higher than crushed granite sold for use as road material. . . .
>
> "As far as we are aware, this is the first case in which respondent has ever argued for such a result. *Reasonable selling expenses are normally considered as costs of mining, not as processing in addition to mining.* See section 1.613-4, Income Tax Regs." (emphasis added)

(ii) The commonly understood meaning of the term "process" in industry does not include selling expenses. Thus, Webster states that the term "process" means:

> "To subject to some special process or treatment . . . To subject (esp. raw material) to a process of manufacture, development, preparation for market, etc.; to convert into marketable form, as livestock by slaughtering, grain by milling, cotton by spinning, milk by pasteurizing, fruits and vegetables by sorting and repacking . . . ." WEBSTER'S NEW INTERNATIONAL DICTIONARY 1972 (2d ed. 1955).

(iii) The statute itself makes clear that the term "process" therein conforms to the above dictionary meaning. As shown by the quotation of subsection 613(c) at p. 36, *supra,* paragraph (2) of said subsection refers to the "treatment processes" described in pagagraph (4). Paragraph (4) is entitled "TREATMENT PROCESSES CONSIDERED AS MINING," and the introduction to that paragraph refers to "The following treatment processes . . . ." Accordingly, it is clear that the reference to "processes" in the kiln feed cut-off established in subparagraph (4)(F) means "treatment processes."

[128] 43 T.C. at 158, 159, n. 13.

Similarly, in *United Salt, supra,* the court stated:[129]

> "To determine the . . . [taxpayer's] 'taxable income from the property' it is evident that '*gross income from the property' must be reduced only by those expenditures which are attributable to the mining stage,* and that some allocation must be made of petitioner's *general, administrative, and selling expenses which apply to both the mining and nonmining stages.* Respondent's regulations recognize the need for this allocation and provide that the allocation should be a fair one." (emphasis added)

One of the two cases on which the Government places its primary reliance in the present action is *Whitehall Cement Mfg. Co. v. United States,* 237 F. Supp. 838 (E.D. Pa. 1965), *affirmed* 369 F.2d 468 (3d Cir. 1966). (The other case is *Standard Lime,* which did not involve selling expenses). In *Whitehall,* the Government's present position on selling expenses was expressly rejected by the District Court in the following statement:[130]

> "*There can be no 'gross income from mining' if there is no sale of the product and there can be few sales without selling expenses.* The government does not appear to contend that plaintiff's selling expenses are unusual in the cement industry or that they would not be incurred by a nonintegrated miner of cement. *Moreover, the government concedes that plaintiff's administrative expenses such as office salaries and expenses are incurred for the benefit of both plaintiff's mining*

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[129] 40 T.C. at 359.
[130] 237 F. Supp. at 843-44.

and manufacturing operations and, that accordingly, these administrative expenses can be allocated between the mining and manufacturing phases of operations in the proportion that the cost of the mining processes before and after the kiln feed point bear to the total direct processing costs. *There appears to be no substantial reason why the two types of expenses should be accorded different treatments.* Accordingly, selling expenses like administrative expenses will be apportioned between mining and manufacturing costs in the proportion that the direct processing costs up to the kiln feed stage bear to the direct processing costs after the kiln feed stage. United Salt Corp., 40 T.C. 359 (1963); North Carolina Granite Corp., 43 T.C. 149 (1964), n. 13." (emphasis added)

The Government did not appeal from this portion of the *Whitehall* trial decision.

The same result was also reached in *Ideal Cement Co. v. United States*, 263 F. Supp. 594 (D.C. Colo. 1966) (appeal to 10th Cir. pending).[131]

Apart from its theory that there should be a presumption in favor of the denominator of the Regulation 118 ratio, the major argument of the Government on selling expenses is that an integrated miner-manufacturer of cement does not incur selling expenses with respect to kiln feed *per se,* because such expenses are incurred only in selling the first marketable product, bulk cement.[132] This obviously negates the entire principle of Regulation 118 and Section 613(c)(4)

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[131] 263 F. Supp at 600-01 (Finding 54 and Conclusion 9).
[132] App. Br. 37.

(F). *Income* is not received with respect to kiln feed, because no one buys kiln feed. Such income must be constructed on a hypothetical basis, by working back from the sales which actually do occur. Similarly, the *expenses* of a nonintegrated producer must also be constructed on a hypothetical basis, by working back from actual sales.

A final contention of the Government is that there is no basis upon which to determine the proper allocation of selling expenses, if in fact such expenses are allocable.[133] This is so spurious that it merits comment only to avoid misleading this Court. All the cases hold that if an item is an indirect, nonprocess expense which benefits the entire mining-manufacturing operation, the basis of allocation shall be in accordance with the ratio of direct mining process costs to total direct mining and manufacturing process costs.[134] This allocation principle is recognized by the Government in this very case by its treatment of general and administrative expenses.[135]

Both Regulation 118 and *Cannelton* make it clear that the starting point for the depletion computation is the full price of the first marketable product. Rev. Rul. 60-98, *supra,* adopts this principle with respect to selling expenses and holds that the sales price of such

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[133] *Id.* at 38.

[134] E.g., *Whitehall, supra,* 237 F. Supp. at 843-44; *Standard Lime, supra,* 329 F.2d at 945:

> ". . . [I]ndirect costs which are incurred for the benefit of the entire operation are . . . . allocated to the first part of taxpayer's operation in the proportion as this part's direct costs bear to the aggregate direct costs."

The Government's own analysis of the depletion computation describes "Step Two" as follows:

> "Allocate Indirect Costs Shown on Cost Classification Sheet between Mining and Nonmining in Proportion to Direct Costs of Each" Def. Ex. A (ex. A thereto, p. 2).

[135] See n. 122, *supra.*

first marketable product is not to be reduced by such expenses. As shown by the table in Appendix B, however, the Government's position with respect to selling expenses provides a smaller depletion allowance than a computation which does reduce the sale price of the first marketable product by all selling expenses.

For the above reasons, we respectfully submit that the Government's position on selling expenses is completely unjustified.

4. California Portland's Alternative Contentions With Respect to Loading and Shipping Costs, and Sacking Costs.

As shown in Plaintiff's Exhibit 5, California Portland incurred expenses of $193,213 at its Colton plant in the representative year 1957 with respect to "loading and shipping applicable to calcined products (bulk equivalent)." The District Court treated this item as exclusively a manufacturing cost,[136] in accordance with the decision of the 1951-52 Case.[137] As previously indicated, California Portland believes that the seven years of litigation in the 1951-52 Case of the same issues here involved should bring an end to this controversy. Accordingly, California Portland is willing to rest on the computation established in that decision, even though there is authority which would treat the substantial item of loading and shipping costs on a basis more favorable than that of the 1951-52 Case and the decision of the District Court. We have cross-appealed on this point only for protective purposes, and seek to raise the alternative contentions set forth below in this section only in the event this Court desires to

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[136]No. 22398, I-R. 213.

[137]No. 18506, R. 25; Pltf. Ex. 9.

reopen and revise the computation of the 1951-52 Case and of the District Court.

The discussion in the previous section with respect to selling expenses appears pertinent to loading and shipping costs, and is incorporated in this section by reference. Loading and shipping is the type of expense referred to as a distribution expense in the case emphasized by the Government, *Standard Lime*,[138] and such a marketing expense appears in many ways analogous to a selling expense. It benefits California Portland's entire mining-manufacturing operation,[139] and is an expense which would be incurred by a nonintegrated miner who performed no manufacturing activities. In fact, in the usual case a nonintegrated miner selling a raw mineral product would have a much higher loading and shipping cost than a taxpayer selling at the end of an integrated mining-manufacturing operation, because of the decrease in bulk occurring when raw mineral is processed into a finished product.

The treatment of loading and shipping costs advocated in this alternative contention was adopted in the *Ideal Cement* decision,[140] and appears to conform to the *Cannelton* principle of equating integrated and nonintegrated miners. California Portland's alternative computations[141] follow the computation method of the 1951-52 Case and of the District Court,

[138]329 F.2d at 948.

[139]Pltf. Ex. 20-C, 369-72; Cf., n. 117, *supra*.

[140]263 F. Supp. at 600-01 (Findings 52(b), 54; Conclusion 9).

[141]Pltf. Ex. 6 and 7; Pltf. Ex. 20-C, 401-03.

except that loading and shipping are allocated to the total mining-manufacturing process instead of being treated as exclusively attributable to manufacturing.[142]

Our position with respect to the incremental costs and revenues of sacking a portion of California Portland's cement is set forth at pp. 30-35, *supra*. In the event that this Court disagrees with the District Court and holds that sacked cement is not a product occurring subsequent to bulk cement, then we believe that the sacking costs and revenues should be allocated to both mining and manufacturing. The evidence establishes that sacking facilitated the sale of a portion of California Portland's cement,[143] and occurred after the processes which produced cement.[144] This alternative treatment of sacking was also adopted by the court in *Ideal Cement*.[145]

5. The Discounts Allowed by California Portland on Sales of Its Cement Were Clearly Cash Discounts and Not Trade Discounts.

The Pre-Trial Conference Order does not provide that California Portland's cash discount practices are an issue in this case.[146] The computation of the Government's principal witness, Mr. Lintz, treats cash dis-

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[142]As an alternative to the treatment of loading and shipping in *Ideal*, it would also be reasonable to follow the treatment of such cost in the Government's principal authority, *Standard Lime*. There, instead of including such cost in the computation as entirely a manufacturing cost, the court took the approach more favorable to the taxpayer of excluding from the computation both the costs and revenues attributable to loading and shipping. 329 F.2d at 948, n. 19.

[143]No. 22398, I-R. 98.

[144]N. 84, *supra*.

[145]263 F. Supp. 600-01 (Finding 51, Conclusion 7).

[146]No. 22398, I-R. 130, 132-33.

counts in a manner which achieves the same dollar result in California Portland's depletion base and depletion allowance as the method of the 1951-52 Case and of the Court below.[147] The Government's attorney expressly represented to the District Court that he would "stand on the Lintz affidavit and its computations," as explained in that affidavit.[148] For these reasons, we strongly objected to the Government's attempt to raise an issue with respect to California Portland's cash discount practices in its post-trial briefs,[149] and we renew that objection here. In addition, the Government has made no allegation that any authority has changed the law respecting cash discounts since the treatment of such item was established in the 1951-52 Case.[150] Since California Portland's practices and the other facts respecting its cash discounts were identical during the years in question with those found in the 1951-52 Case,[151] it is apparent that this point is an *a fortiori* case for application of collateral estoppel.[152] Even if the cash discounts point could be regarded as properly raised and open for relitigation of the 1951-52 result, however, the District Court's treatment of such item in accordance with the 1951-52 Case was clearly correct on the merits.

The District Court made the following finding of fact:[153]

> "13. Plaintiff offered to its customers, after sale, a discount of twenty cents per barrel of ce-

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[147]Def. Ex. A (E.g., ex. A thereto, p. 1).
[148]Tr. 44.
[149]Pltf. Op. Tr. Br. 71-72, 104.
[150]App. Br. 39-42.
[151]No. 22398, I-R. 185-86 (Finding 23).
[152]See pp. 8-9, 23-24, *supra*.
[153]No. 22398, I-R. 182.

> ment. . . . Said discounts were offered by plaintiff for the purpose of inducing prompt payment of plaintiff's invoices and not to induce sales of plaintiff's cement. . . . As practiced and applied during the taxable years . . . [1953-59], such discounts were cash discounts and not trade discounts."

This finding is clearly supported by the evidence.[154]

The distinction between a "cash discount" and a "trade discount" on a product sale is well stated by the Board of Tax Appeals in *American Cigar Co.,* 21 B.T.A. 464 (1930), *Acq.* XI-1 C.B. 1, as follows:[155]

> ". . . A trade discount is the difference between a seller's list prices for his goods and the amount at which he sells those goods to the trade. A cash discount has a very definite meaning also. It is a deduction from the price at which the goods are billed to the purchaser which the seller allows for payment within a certain stated time."

The Government's principal authority, *Standard Lime,* also correctly states the difference between the two types of discounts, as follows:[156]

> "Cash discounts are granted to purchasers in order to encourage prompt payment, thus producing a quicker flow of working capital. They differ from trade discounts in that the latter are granted at the option of the seller no matter when payment is made, depending on market conditions, while the former are availed of entirely at the option of the purchaser."

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[154] Pltf. Ex. 20 C-D, 232-37, 388; Pltf. Ex. 24, p. 4.
[155] 21 B.T.A. at 499.
[156] 329 F.2d at 947, n. 18.

The *Standard Lime* treatment of cash discounts[157] is in essence the same as the method of the District Court,[158] of the 1951-52 Case,[159] and of the Government's principal witness, Lintz.[160] It is also the same as that developed in *Riverside Cement Co. v. United States,* 58-2 USTC para. 9905 (S.D. Cal. 1958). In reaching this result, the *Standard Lime* court made the following statement, which is equally pertinent here:[161]

> "The Government contends that no part of this [cash discount] expense may be allocated to mining since '[n]o part of this expense was incurred at the end of mining when taxpayer theoretically sold the kiln feed to its manufacturing alter ego.' The Government's contention fails to envision the purpose for which these expense items serve. Taxpayer's experts testified that the function of a cash discount is to stimulate prompt payment in order to assure a quicker flow of working capital. It is a financial expense which is incurred for the benefit of both stages of the production process since it is obvious that working capital is needed for both the mining and manufacturing processes. Consequently, we must hold that cash discounts are an indirect expense which are incurred for the benefit of the entire operation and as such can be properly allocated in taxpayer's computation of gross income from the property at kiln feed."

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[157] 329 F.2d at 947-48.

[158] No. 22398, I-R. 182, 186, 189 (Findings 13, 24; Conclusion 6); p. 39, *supra.*

[159] No. 18506, R. 12, 18, 20-21 (Finding 13, 20; Conclusion 7); Pltf. Ex. 9.

[160] N. 147, *supra.*

[161] N. 157, *supra.*

6. The Principal Authority Cited by the Government Does Not Support Its Position.

The Government alleges that the *Standard Lime* decision justifies a reopening of the 1951-52 Case computation and supports its present litigation theories.[162] Analysis of *Standard Lime* shows that this is simply not true.

(a) The Government contends that California Portland's costs of sacking a portion of its cement is a manufacturing cost and should be placed in the denominator of the depletion computation. We have shown that this treatment violates the express "first marketable product" requirement of Regulation 118, and results in two different constructive prices for the single, fungible product of kiln feed. The *Standard Lime* court regarded packing and loading costs of bulk cement to be analogous to the cost of sacking cement,[163] and had this to say about such costs:

> "If considered a direct non-mining expense, this would increase the denominator of the formula, *supra,* thus having a greater reducing effect in taxpayer's gross income from the property at kiln feed. *We cannot consider these items direct non-mining costs* since we have accepted taxpayer's expert's opinion concerning the point at which the mining-manufacturing processes cease."[164] (emphasis added)

The actual judgment computation of *Standard Lime*[165] eliminated $149,413.50 of "bag premium" from "gross income from cement," and under the heading "Bag Premium Cost Elimination," eliminated $146,180.55 of

[162] App. Br. 24-25, 33, 38-39; Def. R. Tr. Br. 3.

[163] 329 F.2d at 948-49.

[164] 329 F.2d at 948, n. 19.

[165] Pltf. Ex. 1.

the cost of "containers" from the costs included in the Regulation 118 computation. *This elimination from the depletion computation of both the costs and revenues of sacking is exactly the procedure followed in the 1951-52 Case and by the District Court here.*

(b) Selling costs, which are one of the Government's major points of contention in the present case, were not involved in *Standard Lime.*[166]

(c) The Government alleges that loading and shipping costs are exclusively a manufacturing cost. As noted above, the *Standard Lime* court specifically rejected the Government's position on this point.

(d) As also discussed above, *Standard Lime* is direct authority against the Government's position on cash discounts, and completely supports the decision of the District Court on this point.

The Government's other main authority is *Whitehall Cement.* That case completely denies the Government's present position on selling expenses.[167] It is, however, the only case cited by the Government which supports its position on sacking costs. The only argument made by the *Whitehall* taxpayer on this point was that the incremental income received from the sale of cement in sacks was less than the cost of sacking. The Court held this argument invalid, because if *all* the costs and revenues attributable to sacked cement were considered, the sale of that product did not result in a loss.[168] In the present case the District Court specifically found as a fact that California Portland's first marketable product was bulk cement.[169] If the same finding had

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166 See the statement of issues at 329 F.2d 942.

167 Pp. 51-52, *supra.*

168 369 F.2d at 473-74.

169 No. 22398, I-R. 184-85 (Finding 21).

existed in *Whitehall,* and that court had been advised of the specific requirement in Regulation 118 that the taxpayer's first marketable product be used as the computation's starting point, we submit that *Whitehall* would have reached the same result as the great weight of authority discussed above.[170] This is particularly true since the *Whitehall* court was also not advised that the Government's position results in two different constructive values for the same fungible product—kiln feed.

For the foregoing reasons, we respectfully submit that every element of the District Court's depletion computation discussed in the sections above is fully supported by the 1951-52 Case, and by the overwhelming weight of all other pertinent authority.

7. California Portland's Handling Costs of Pre-kiln Additives Are Clearly Attributable to Its Mining Processes.

The remaining question in this case is minor, and concerns the $14,851 item in Plaintiff's Exhibit 5 for the representative year 1957 entitled "Costs of handling additives used prior to cutoff point." On this point, the District Court made the following finding of fact:[171]

> "14. The mineral materials iron ore and quartzite were added by plaintiff to its calcium carbonate rock in the production of its cement clinker and finished cement. Said minerals were added in the raw grinding stage prior to the introduction of the raw mix into the kiln, and such process was an essential step in the production of cement clinker and finished cement from plaintiff's cal-

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[170]Pp. 30-35, *supra.*

[171]No. 22398, I-R, 182-83.

cium carbonate rock. Subsequent to acquisition by plaintiff but prior to actual admixture with plaintiff's calcium carbonate rock, said mineral materials were stored on plaintiff's premises and then moved to the point of admixture. Such storage and handling was a necessary part of the process of mixing said mineral materials with plaintiff's calcium carbonate rock prior to introduction into the kiln, and the cost of such storage and handling should be treated as a mining cost under the formula described in paragraph 18 of these Findings of Fact."

The Government does not dispute this finding, except for the conclusion that the costs of storing and handling pre-kiln additives is a mining cost.[172]

California Portland conceded at the trial that it was not entitled to depletion on the costs of acquiring the minerals used as additives to its in-process calcium carbonate rock prior to introduction of the kiln feed into the kiln. Accordingly, it asked the District Court to exclude from its depletion base the total acquisition cost of such additives up to the time it received delivery thereof at its cement plant. The Government admitted that the costs of blending or physically mixing such additives with California Portland's in-process calcium carbonate rock prior to the kiln feed stage was a "mining" cost.[173] The only controversy concerned the proper depletion treatment of the costs of handling these additives between the time they were delivered to California Portland's cement plant and the time they were physically mixed with its in-process

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[172]App. Br. 7-8.

[173]Tr. 19-20. See also, *Riddell v. California Portland Cement Co., supra,* 330 F.2d at 18.

calcium carbonate rock.[174] Such handling costs consisted primarily of storage until the additives were needed for use, and of physically moving the additives from the place of receipt at California Portland's plant to the place in said plant of blending and mixing with the in-process calcium carbonate rock.[175]

Subparagraph (F) of Section 613(c)(4) provides that California Portland is entitled to depletion on:

> ". . . all processes (other than preheating of the kiln feed) applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process."

Paragraph (5) of Section 613(c) provides:

> ". . . Unless such processes are otherwise provided for in paragraph (4) (*or are necessary or incidental to processes so provided for*), the following treatment processes shall not be considered as mining'. . . ." (emphasis added)

Prior to the adoption by Congress of the kiln feed cutoff point, the Government took the following position in its *Rev. Rul.* 290:[176]

> "It is the position of the Internal Revenue Service that calcium carbonates and shale, mined for use in the cement industry, are not customarily

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[174]Tr. 19-20; Pltf. Ex. 20-B 210, 212.

[175]*Ibid.*

[176]1953-2 C.B. 41. This ruling, which primarily established a cutoff point for cement manufacturers after the raw grinding stage and prior to the kiln feed stage, was revoked after *Cannelton*. See *Rev. Rul.* 61-17, 1961-1 C.B. 8. A change in the cutoff point between "mining" and "manufacturing" does not affect the question of additives introduced at a point which all agree is "mining." The continued validity of the principle of *Rev. Rul.* 290 with respect to additives was expressly recognized by this Court on the second appeal of the 1951-52 Case. See p. 65, ***infra.***

> sold in the form of the crude mineral product, and that, therefore, under . . . [Regulation 118], crushing and grinding are considered 'ordinary treatment processes' in the computation of gross income from the property for percentage depletion purposes. Blending with other material after crushing and grinding, such as that occurring at the kiln feed bins, is excluded from 'ordinary treatment processes,' but *where mixing of the calcium carbonates and shale occurs before crushing and grinding, it will be considered as incidental to such processes.*
>
> *"The gross income for percentage depletion purposes must of course be computed separately with respect to each component mineral, notwithstanding any such mixing. . . ."* (emphasis added)

In the second appeal of the 1951-52 Case, this Court commented on *Rev. Rul.* 290 and the subsequent adoption by Congress of the kiln feed cutoff point as follows:[177]

> "We believe that by the enactment of the amendment in question Congress intended only to move the cutoff point from the crushing and grinding stage to the pre-kiln stage, but not to alter the revenue ruling with respect to separate computation of depletion of component minerals. To hold otherwise would be to allow a double deduction on the iron ore extracted by the taxpayer. . . . Surely Congress did not mean to grant the additional relief of allowing depletion upon minerals already depleted. . . ."

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[177] *Riddell v. California Portland Cement Co.*, 330 F.2d 16, 18-19 (9th Cir. 1964).

The above authorities establish that activities "necessary or incidental" to "ordinary treatment processes" are attributable to "mining," but that both the seller and the purchaser of a mineral are not each entitled to the same depletion deduction with respect to that mineral.

In the present case, it is clear that the miner of the additives acquired by California Portland is entitled to depletion on the sales price or value of such additives, and that the District Court's computation has entirely eliminated such price or value from California Portland's depletion base. At the same time (as testified by the Government's witnesses,[178] as evidenced by the small amount concerned, and as specifically found by the District Court), the use of these pre-kiln additives is obviously only most incidental to California Portland's mining processes.[179] Accordingly, on the rationale and results of the above authorities, it is clear that the "handling costs of additives" here concerned are much more analogous to the blending activities, which the Government admits are part of California Portland's depletion base, than to the taking of a double depletion deduction with respect to the same mineral which this Court forbids.

The Government's principal argument against the above conclusion appears to be that said handling and storage costs are costs of "processes" applied to the additives themselves, rather than to California Portland's calicum carbonate rock.[180] It is clear, however, that the only "process" here concerned is that of

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[178]Pltf. Ex. 19, 29, 62, 112-15.

[179]*Accord, Ideal Cement, supra,* 263 F. Supp. at 601 (Finding 61).

[180]App. Br. 26-27.

blending the pre-kiln additives with the calcium carbonate rock—a process which the Government admits is "mining." Certainly the cost of placing the additives in a position so that they may be blended is necessary and incidental to the blending process.

Conclusion.

The District Court's depletion computation is supported, pursuant to the principles of collateral estoppel and *stare decisis,* by exactly the same result on the same facts in the 1951-52 Case. In addition, the District Court's decision is also supported in all respects by the overwhelming weight of the other pertinent authorities. Accordingly, we respectfully request that the judgment below be affirmed.

Respectfully submitted,

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Counsel for California Portland Cement Company.

April, 1968

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

STUART T. PEELER

APPENDIX A.

Internal Revenue Code of 1954:

SEC. 611. ALLOWANCE OF DEDUCTION FOR DEPLETION.

(a) *General rule.*—In the case of mines, oil and gas wells, other natural deposits, and timber, there shall be allowed as a deduction in computing taxable income a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under regulations prescribed by the Secretary or his delegate. * * *

* * * *

(26 U.S.C.A. § 611, West's 1967 ed.)

SEC. 613. PERCENTAGE DEPLETION.

(a) *General rule.*—In the case of the mines, wells, and other natural deposits listed in subsection (b), the allowance for depletion under section 611 shall be the percentage, specified in subsection (b), of the gross income from the property excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 percent of the taxpayer's taxable income from the property (computed without allowance for depletion). * * *

(b) *Percentage depletion rates.*—The mines, wells, and other natural deposits, and the percentages, referred to in subsection (a) are as follows:

* * * *

(7) 15 percent—all other minerals (including, but not limited to * * * calcium carbonates * * *)

* * * *

(c) *Definition of gross income from property.*—For purposes of this section—

(1) *Gross income from the property.*—The term "gross income from the property" means, in the case of a property other than an oil or gas well, the gross income from mining.

(2) *Mining.*—The term "mining" includes not merely the extraction of the ores or minerals from the ground but also the treatment processes considered as mining described in paragraph (4) (and the treatment processes necessary or incidental thereto) * * *.[1]

* * * *

(4) *Treatment processes considered as mining.*—The following treatment processes where applied by the mine owner or operator shall be considered as mining to the extent they are applied to the ore or mineral in respect of which he is entitled to a deduction for depletion under section 611:

* * * *

(F) in the case of calcium carbonates and other minerals when used in making cement—all processes (other than preheating of the kiln feed) applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process;

* * * *

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[1]The quotation of § 613(c)(2) in the Appendix to the Government's brief appears erroneous. Such quotation does not reflect the 1960 amendment to said § 613(c)(2), which is applicable here.

(26 U.S.C.A. § 614, West's 1967 ed.)

Public Debt and Tax Rate Extension Act of 1960, P.L. 86-564, 74 Stat. 290:

SEC. 302. DEPLETION RATE FOR CERTAIN CLAYS; TREATMENT PROCESSES CONSIDERED AS MINING FOR COMPUTING PERCENTAGE DEPLETION IN THE CASE OF MINERALS AND ORES.

* * * *

(b) *Treatment Processes Considered as Mining.*—Subsection (c) of section 613 of the Internal Revenue Code of 1954 (relating to the definition of gross income from property) is amended as follows:

(1) By amending paragraph (2) to read as follows:

"(2) *Mining.*—The term 'mining' includes not merely the extraction of the ores or minerals from the ground but also the treatment processes considered as mining described in paragraph (4) (and the treatment processes necessary or incidental thereto) * * *."

(2) By striking out paragraph (4) and inserting in lieu thereof the following new paragraphs:

"(4) *Treatment processes considered as mining.*—The following treatment processes where applied by the mine owner or operator shall be considered as mining to the extent they are applied to the ore or mineral in respect of which he is entitled to a deduction for depletion under section 611:

* * * *

"(F) in the case of calcium carbonates and other minerals when used in making cement —all processes (other than preheating of the kiln feed) applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process;

* * * *"

(c) *Effective Date.*—The amendments made by subsections (a) and (b) shall be applicable only with respect to taxable years beginning after December 31, 1960.

Act of September 14, 1960, P.L. 86-781, 74 Stat. 1017:

SEC. 4. Subsection (c) of section 302 of the Public Debt and Tax Rate Extension Act of 1960 (Public Law 86-564; 74 Stat. 293) is amended to read as follows:

"(c) *Effective Date.*—

"(1) *In general.*—Except as provided in paragraph (2), the amendments made by subsections (a) and (b) shall be applicable only with respect to taxable years beginning after December 31, 1960.

"(2) *Calcium carbonates, etc.*—

"(A) *Election for past years.*—In the case of calcium carbonates or other minerals when used in making cement, if an election is made by the taxpayer under subparagraph (c)—

"(i) the amendments made by subsection (b) shall apply to taxable years with respect to which such election is effective, and

"(ii) provisions having the same effect as the amendments made by subsection (b) shall be deemed to be included in the Internal Reve-

nue Code of 1939 and shall apply to taxable years with respect to which such election is effective in lieu of the corresponding provisions of such Code.

"(B) *Years to which applicable.*—An election made under subparagraph (C) to have the provisions of this paragraph apply shall be effective for all taxable years beginning before January 1, 1961, in respect of which—

"(i) the assessment of a deficiency,

"(ii) the refund or credit of an overpayment, or

"(iii) the commencement of a suit for recovery of a refund under Section 7405 of the Internal Revenue Code of 1954,

is not prevented on the date of the enactment of this paragraph by the operation of any law or rule of law. Such election shall also be effective for any taxable year beginning before January 1, 1961, in respect of which an assessment of a deficiency has been made but not collected on or before the date of the enactment of this paragraph.

* * * *"

Treasury Regulations on Income Tax (1954 Code):

SEC. 1.9003-2

Effect of election.

(a) *In general.* If a taxpayer makes the election described in paragraph (b) of Section 1.9003-1, he shall be deemed to have consented to the application of section 302(b) of the Act with respect to all taxable years to which the election applies. Thus, subparagraph (F) of section 613(c)(4) of the Internal

Revenue Code of 1954 as amended must be applied in determining gross income from mining for the taxable years to which the election applies (including years subject to the Internal Revenue Code of 1939) whether or not the taxpayer is litigating the issue. Further, the election shall apply to all calcium carbonates or other minerals mined and used by the taxpayer in making cement.

* * * *

(26 C.F.R. Sec. 1.9003-2.)

Treasury Regulations 118 (1939 Code):

SEC. 39.23(m)-1. *Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.*

* * * *

(e) As used in sections 114(b)(3) and 114 (b)(4)(A) and sections 39.23(m)-1 to 39.23(m)-19, inclusive, the term "gross income from the property" means the following:

* * * *

(2) In the case of a crude mineral product other than oil and gas, "gross income from the property," as used in section 114(b)(4)(A), means the gross income from mining. The term "mining" as used herein includes not only the extraction of ores or minerals from the ground but also the ordinary treatment processes which are normally applied by the mine owners or operators to the crude mineral product after extraction in order to obtain the commercially marketable mineral product or products.

* * * *

(3) If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold, but, if the product is transported or processed (other than by the ordinary treatment processes described below) before sale, "gross income from the property" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes actually applied, before transportation of such product (other than transportation treated, for the taxable year, as mining). If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude mineral state is merely transported the price for which sold) minus the costs and proportionate profits attributable to the transportation (other than transportaion treated, for the taxable year, as mining) and the processes beyond the ordinary treatment processes. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

* * * *

APPENDIX B.

Treatment of Selling Expense as Exclusively Attributable to Manufacturing.

	Examples 1	2	3	4	5	6
Selling price	$100	$100	$100	$100	$100	$100
Pre cut-off cost	10	20	30	40	50	60
Post cut-off cost						
Selling expense	10	15	20	15	10	5
Other	60	50	40	30	20	10
Total post cut-off cost	70	65	60	45	30	15
Total cost	80	85	90	85	80	75
Cut-off ratio	10/80	20/85	30/90	40/85	50/80	60/
Gross income from mining	$12.50	$23.53	$33.33	$47.06	$62.50	$80

Selling Price of First Marketable Product Reduced by Selling Expenses.

	1	2	3	4	5	6
Selling Price	$100	$100	$100	$100	$100	$100
Less selling expense	(10)	(15)	(20)	(15)	(10)	(5
Selling price as adjusted	90	85	80	85	90	95
Pre cut-off cost	10	20	30	40	50	60
Post cut-off cost	60	50	40	30	20	10
Total cost	70	70	70	70	70	70
Cut-off ratio	10/70	20/70	30/70	40/70	50/70	60/
Gross income from mining	$12.86	$24.29	$34.29	$48.57	$64.29	$81

Nos. 22397-22398A

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

No. 22397

UNITED STATES OF AMERICA,

Appellant,

vs.

CALIFORNIA PORTLAND CEMENT COMPANY, a corporation, Successor-in-Interest to ARIZONA PORTLAND CEMENT COMPANY, a corporation,

Appellee.

No. 22397-A

CALIFORNIA PORTLAND CEMENT COMPANY, a corporation, Successor-in-Interest to ARIZONA PORTLAND CEMENT COMPANY, a corporation,

Cross-Appellee,

vs.

UNITED STATES OF AMERICA,

Cross-Appellant.

No. 22398

UNITED STATES OF AMERICA,

Appellant,

vs.

CALIFORNIA PORTLAND CEMENT COMPANY,

Appellee.

No. 22398-A

CALIFORNIA PORTLAND CEMENT COMPANY,

Cross-Appellant,

vs.

UNITED STATES OF AMERICA,

Cross-Appellee.

Closing Brief for California Portland Cement Company.

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Nos. 22397-22398A

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

No. 22397

UNITED STATES OF AMERICA,

Appellant,

vs.

CALIFORNIA PORTLAND CEMENT COMPANY, a corporation, Successor-in-Interest to ARIZONA PORTLAND CEMENT COMPANY, a corporation,

Appellee.

No. 22397-A

CALIFORNIA PORTLAND CEMENT COMPANY, a corporation, Successor-in-Interest to ARIZONA PORTLAND CEMENT COMPANY, a corporation,

Cross-Appellee,

vs.

UNITED STATES OF AMERICA,

Cross-Appellant.

No. 22398

UNITED STATES OF AMERICA,

Appellant,

vs.

CALIFORNIA PORTLAND CEMENT COMPANY,

Appellee.

No. 22398-A

CALIFORNIA PORTLAND CEMENT COMPANY,

Cross-Appellant,

vs.

UNITED STATES OF AMERICA,

Cross-Appellee.

Closing Brief for California Portland Cement Company.

The Government's closing brief provides an excellent illustration of the reasoning by which it ignores seven years of prior litigation, the purpose of the depletion computation, and the pertinent authorities.

A. The Alleged Untimeliness of California Portland's Cross-Appeals.

The judgments of the District Court became final on July 31, 1967. The Government appealed on September 28, 1967 and California Portland cross-appealed on October 6, 1967.[1] In its closing brief, the Government alleges that California Portland's notices of appeal "may" have been untimely.[2] In making this allegation, the Government entirely disregards FED. R. CIV. PROC. 73(a) which specifically provides:

> ". . . (3) if a timely notice of appeal is filed by a party, any other party may file a notice of appeal within 14 days of the date on which the first notice of appeal was filed. . . ."[3]

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[1]C.P.C. Op. Br. 2, nn. 1-3.

[2]Gov't. Cl. Br. 2 (n. 2), f. 6.

[3]The Government's citation of 28 U.S.C. §2107 is misleading. Prior to the 1966 amendments to the Federal Rules, the appeal period for both parties where the United States was a litigant was 60 days. 7 MOORE, FEDERAL PRACTICE 3125 (1966). Section 2107 of Title 28, U.S.C., enacted in 1948, reflected this rule. From the date of enactment of the Federal Rules, however, the law has been that each time a new Federal Rule is promulgated, conforming changes will not necessarily be made in the Judicial Code or other applicable statutes and, in case of conflict, the revised Federal Rule will supersede a prior inconsistent statute. The purpose of this is to avoid the burden of amending all pertinent statutes each time a Federal Rule is enacted or amended, and to avoid confusion in case all of the relevant statutes are not amended each time a Federal Rule is changed. See MOORE, *supra,* vol. 2 pp. 128-31, vol. 7A pp. 22-23. Accordingly, the Government is completely unjustified in suggesting that a prior statute controls the 1966 amendment to Federal Rule 73(a). See 28 U.S.C. §2072; *McConville v. United States,* 197 F.2d 680, 682 (2d Cir. 1952).

B. The Government's Procedural Attempt to Avoid Collateral Estoppel.

The Government next alleges that the "primary" contention in our opening brief is that it is collaterally estopped from its present relitigation, that we have presented our collateral estoppel argument by cross-appeal, and that this argument was not preserved in our notices of appeal.[4]

Of our total opening argument of 60 pages, 17 pages concerned collateral estoppel and 43 pages were devoted to the merits. As therein clearly stated, our position is that the District Court's judgment is supported by both collateral estoppel and the merits, and that either analysis compels affirmance.[5]

In addition, our opening brief also makes it clear that we do not present the collateral estoppel argument by cross-appeal.[6] We do not seek to change a single particular of the District Court's judgment on this ground, but instead contend that collateral estoppel supports that judgment in all respects. It is hornbook law that an appellee may raise any legal argument in support of the judgment of the trial court, regardless of whether such argument was relied upon or even considered by the court below. E.g., *White v. Higgins*, 116 F.2d 312, 318 (1st Cir. 1940).

Along with its disregard of our brief, the Government again ignores Federal Rule 73 which provides: ". . . (b) the notice of appeal shall . . . designate *the judgment* or part thereof appealed from. . . ."

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[4]Gov't. Cl. Br. 3, 4, 6.

[5]See, e.g., C.P.C. Op. Br. 6-7.

[6]E.g., *id.* at 5-6.

(emphasis added) Here, the judgment of the District Court applied the exact depletion computation developed in the 1951-52 Case[7] and, except for California Portland's alternative computation which *is* raised by cross-appeal, provided California Portland with the precise amount of refund requested. As stated by this Court, ". . . an appeal lies from a judgment, not from findings. . . . In order that a judgment be appealable at the behest of a party, the party must be aggrieved by it." *United States v. Adamant Co.,* 197 F.2d 1 (9th Cir. 1952).

Implicit in the Government's position is the contention that a notice of appeal must specify not only the judgment appealed from, but also the alleged subsidiary errors of the trial court. Although it is not in accordance with law, we are willing to submit to this view, provided the Government is similarly bound. In such case, however, the Government has no standing to make any argument on the merits to this Court, because its notices of appeal specified only the judgments (as distinguished from the numerous factual and legal rulings) which were adverse to it.[8]

C. The Government's Substantive Attempt to Avoid Collateral Estoppel.

1. *The alleged differences in the facts.* The Government's first claim is that there is not a requisite identity of facts between the 1951-52 Case and the present case.[9] In this connection, it appears to argue that for collateral estoppel to apply to *any* issue which is common to the two cases, all of the facts and all

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[7]See n. 40, *infra.*

[8]No. 22397, I-R. 163; No. 22398, I-R. 238.

[9]Gov't. Cl. Br. 8-10.

of the issues in the two cases must be identical.[10] This, of course, is not the law. It is well established that collateral estoppel can apply to a single common issue between two cases, even if all other facts and issues are different and collateral estoppel is inapplicable to such other facts and issues. See, e.g., *Commissioner v. Sunnen*, 333 U.S. 591, 598 (1947); 1B MOORE, FEDERAL PRACTICE 3851-53 (1965).

The Government states that the present case involves "two sites, Colton and Mojave,"[11] while the 1951-52 Case involved only Colton. If this distinction has meaning, it still does not affect collateral estoppel as to the depletion computation at Colton (which represents the major part of the amount now in controversy). As discussed in our opening brief,[12] the Colton Quarry is common to both the 1951-52 Case and this case, and the facts relevant to its depletion computation were no different in 1953-59 than in 1951-52.

In addition, the operations and pertinent facts at Mojave and Rillito were the same as at Colton during 1951-52,[13] and therefore the depletion computation applicable to Colton should also be applicable to the other two quarries, either by collateral estoppel or by *stare decisis*.[14] The Government itself recognizes this in its identical treatment of the three quarries in all of its arguments.[15]

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[10]*Id.* at 9-10.

[11]*Id.* at 9.

[12]E.g., C.P.C. Op. Br. 8-9.

[13]No. 22397, I-R. 81, 125-26; No. 22398, I-R. 117, 185-86.

[14]See, e.g., C.P.C. Op. Br. 22-24.

[15]See also the Government's admission that: "The material facts and documents in each of these cases are substantially identical." Gov't. Op. Tr. Br. 3, n. 1.

The second allegation of difference is that "the District Court did *not* find (as it did with respect to some issues) that the facts and circumstances relevant to handling additives were the same in both cases."[16] This is not only inaccurate,[17] but it is also irrelevant, because we do not contend that the Government is collaterally estopped on this one *de minimus* point.

The final allegation of factual difference between the two cases is the Government's claim that California Portland's cash discount practices were not the same in 1953-59 as they were in 1951-52.[18] The District Court expressly found to the contrary,[19] pursuant to the uncontroverted testimony of California Portland's controller.[20] The Government's contention that this finding was "clear error" is unsupported by any evidence of change in discount practices between the two periods.

2. *The claimed settlement.* The Government next claims that the entire judgment in the 1951-52 Case was a compromise, "with a reservation of the Government's right to relitigate."[21] The complete disregard of the facts surrounding this assertion has been fully discussed in our opening brief.[22] This is also evident from the two quotations cited in the Government's

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[16]Gov't. Cl. Br. 9.

[17]The District Court followed the treatment of such handling costs adopted in the 1951-52 Case, and specifically found that the relevant facts pertaining to production of cement were the same in 1953-59 as in 1951-52. E.g., No. 22398, I-R. 185-86.

[18]Gov't. Cl. Br. 9-10, n. 4.

[19]No. 22398, I-R. 185-86; No. 22397, I-R. 125.

[20]*Id.* at 98-99.

[21]Gov't. Cl. Br. 5, 9, 11, 12, 13.

[22]C.P.C. Op. Br. 9-18.

own brief. The first such quotation (of the Government's own counsel) expressly recognizes:

> "*If the collateral estoppel principle is against us,* it will be as a matter of law rather than by my agreement."[23] (emphasis added)

Clearly the Government's counsel was aware that the final judgment in the 1951-52 Case could be the basis for collateral estoppel in a future proceeding, "as a matter of law."

The Government's second quotation (from the stipulation to re-entry of the unappealed 1962 findings and conclusions) describes the usual status of a judgment entered after judicial determination of a controversy. In such case, the losing party does not by the entry of judgment "[waive] his objection thereto nor . . . concede the correctness thereof [,] either for the taxable years in suit or subsequent taxable years."[24] Instead he is free to directly attack the judgment by appeal,[25] or, in certain limited circumstances, by a collateral attack in a separate proceeding. It is only where his agreement does waive his objections and does concede the correctness of the judgment that the case is settled by compromise.[26] It should therefore be beyond controversy that the only point "compromised" in the 1951-52 Case was that of the handling costs of pre-kiln additives.

3. *The claimed changes in the law.* The Government's main assertion against collateral estoppel is that

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[23]Gov't. Cl. Br. 11.

[24]*Ibid.*

[25]As occurred here. See Pltf. Ex. 10.

[26]See, e.g., *Swift & Co. v. United States*, 276 U.S. 311, 323-24 (1927).

there have been "intervening changes in the law"[27] since the judgment in the 1951-52 Case. This argument contains, *inter alia,* the following errors:

(i) The premise that "the pertinent changes are those occurring after October 8, 1962."[28] This ignores the two appeals to this Court after that date, the fact that a final decision was not obtained until February 16, 1965, and the Government's own position that the 1965 judgment controls for collateral estoppel purposes because it was a "compromise."

(ii) The premise that only a "subtle change"[29] in the law will prevent collateral estoppel. If this were true, a litigant could almost always show such a "subtle change" by a slightly different result in some other forum somewhere, and the doctrine of collateral estoppel would not exist. As discussed in our opening brief,[30] the actual requirement stated by the courts is "a decisive change in the law"[31] and "an intervening legal development . . . which makes manifest the error of the result reached . . . [in the earlier case]."[32] The cases cited by the Government affirm this standard.[33]

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[27]Gov't. Cl. Br. 12-21.

[28]*Id.* at 12.

[29]*Id.* at 7.

[30]C.P.C. Op. Br. 19-20, n. 51.

[31]*Lynch v. Commissioner,* 216 F.2d 574, 580 (7th Cir. 1954).

[32]*Commissioner v. Sunnen,* 333 U.S. 591, 603 (1948).

[33]In *Sunnen,* the landmark *Clifford-Horst* line of decisions had greatly altered the tax law of intra-family transactions between the date of the judgment claimed to have collateral estoppel effect and the second suit. In *McCall v. Commissioner,*

(This footnote is continued on the next page)

(iii) The allegation that the law is now different from that applied in the 1951-52 Case.[34] Assuming *arguendo* that the relevant date is October 8, 1962, the first alleged change[35] is *Riddell v. Monolith Portland Cement Co.*, 371 U.S. 537 (1963). *Monolith* held that cement producers could not use their end product as the depletion base, because *Cannelton* was applicable to them. This was exactly the principle on which the 1962 judgment in the 1951-52 Case was based. The parties recognized the applicability of *Cannelton* on the first appeal of the 1951-52 Case, and the 1962 judgment was entered pursuant to this Court's instructions for the District Court to formulate a depletion computation using the same kiln feed depletion base applicable here. *Riddell v. California Portland Cement Co.*, 297 F.2d 345, 355, (9th Cir. 1962).

The Government then cites four cases without comment. They are not pertinent and are discussed by footnote.[36]

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312 F.2d 699 (4th Cir. 1963), the first case determined that the taxpayers had a depletable interest under a lease, without considering the effect of a 30-day cancellation clause. Thereafter the Supreme Court held that such a cancellation clause was controlling and precluded the right to depletion. In *CBN Corporation v. United States*, 364 F.2d 393 (Ct. Cl. 1966), *cert. denied*, 386 U.S. 981 (1967), the court stated that its own intervening *Tidewater* decision had made "a marked alteration in approach to the problem at hand" and a "change of course in our approach to depletion matters." 364 F.2d at 396.

[34]"In sum, the state of the law and legal climate is vastly different today from its state in 1962." Gov't. Cl. Br. 21.

[35]Gov't. Cl. Br. 14-15.

[36]The four cases (cited at pp. 15-16) are *United States v. Portland Cement Co. of Utah*, 315 F.2d 169 (10th Cir. 1963);

(This footnote is continued on the next page)

The remaining cases cited by the Government are *Standard Lime* and *Whitehall.* These are discussed in our opening brief and, as established there,[37] support the 1951-52 Case computation far more than the Government's present litigation theories.

(iv) Finally, the Government neglects to mention that the great weight of authority supports the 1951-52 Case computation.[38]

D. Miscellaneous Misstatements by the Government.

Among the many other inaccuracies in the Government's closing brief are the following:

1. The amazing statement that nothing in the record supports our "assertion" that the District Court followed the depletion computation formulated in the 1951-52 Case.[39] The applicability of the 1951-52

United States v. Longhorn Portland Cement Co., 328 F.2d 491 (5th Cir. 1964); *United States v. Light Aggregates, Inc.,* 343 F.2d 429 (8th Cir. 1965); and *Solite Corporation v. United States,* 375 F.2d 684 (4th Cir. 1967). The issue in each was whether the taxpayer's depletion base was its finished end product or an earlier stage of production. As stated in the text, California Portland's depletion base was established at the kiln feed point prior to both the 1962 and 1965 judgments, and therefore these cases also constituted no "change in the law" applicable to said judgments.

The Government also cites two subsequent opinions in the *Portland of Utah* litigation, appearing at 338 F.2d 798 (1964) and 378 F.2d 91 (1967). Such opinions involved the question of whether the proportionate profits method of Reg. 118 was applicable, and eventually concluded it was. This, of course, was exactly the method applied in the 1962 and 1965 judgments in the 1951-52 Case.

[37]See, e.g., C.P.C. Op. Br. 60-62.

[38]*Id.* at 25-67.

[39]Gov't. Cl. Br. 6, n. 3.

Case computation was our principal argument below, as it is here. The District Court's computation is identical in every detailed particular (except for dollar amounts) with the method established in the 1951-52 Case.[40]

2. The statement that after the alleged "compromise" judgment in the 1951-52 Case, "an appeal was never intended, authorized or docketed."[41] The Government's Notice of Appeal is in evidence as Pltf. Ex. 10, as is the Government's "Motion for Extension of Time to Designate Record and Docket Cause on Appeal and Order."

3. The surprising statement that the "first marketable product" is not the starting point for the Regulation 118 computation.[42] This ignores the express language of the Regulation, which could not be more explicit:

> ". . . [T]here shall be used . . . the representative market or field price *of the first marketable product* resulting from any process or processes . . . minus the costs and proportionate profits attributable to the . . . processes beyond the ordinary treatment processes." (emphasis added)

It also ignores the Government's own position in its opening brief that California Portland's "first marketable product"[43] was *both* bulk and sacked cement.

4. The assertion that *Standard Lime* and *Whitehall* "are in accord" on the treatment of bags and bagging.[44]

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[40]No. 22397, I-R. 88; No. 22398, I-R. 128; C.P.C. Op. Br. 5, n. 16.

[41]Gov't. Cl. Br. 12, n. 5.

[42]*Id.* at 25.

[43]Gov't. Op. Br. 34.

[44]Gov't. Cl. Br. 24.

In its discussion of *Standard Lime,* the Government states that the Court of Claims held that sacking costs were "non-mining costs in their entirety."[45] It fails to recognize, however, that this does not answer the depletion computation question. If a miner of calcium carbonates sold one-half of its production as bulk cement and used the other half to construct buildings which it then sold, obviously the construction costs would be "non-mining." It is also obvious, however, that such construction costs should not be placed in the denominator of the depletion computation. Instead, the Regulation expressly requires that the computation be developed from the "first marketable product." This is exactly what was done in *Standard Lime,* and there the incremental costs and revenues of the *subsequent product* of sacked cement were eliminated in exactly the same manner as that of the court below.[46]

5. The contention that certain authorities cited in our opening brief with respect to sacking are not in point because "they involve determinations, with respect to unintegrated miners, as to their 'commercially marketable * * * product' of mining processes."[47] If the courts eliminate the incremental costs and revenues of sacking in determining the "commercially marketable product," this result is *a fortiori* where the Regulation expressly requires reference to the "*first* marketable product."

6. The statement that California Portland's alternative computation is "untimely" and seeks "entirely

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[45]*Id.* at 17.
[46]Pltf. Ex. 1; C.P.C. Op. Br. 60-61.
[47]Gov't. Cl. Br. 26.

different relief."[48] The relief sought in this case is a depletion computation which the Government will be required to accept. Our basic position is that the method established for 1951-52 remains applicable to 1953-59. When the Government introduced new computation theories at the trial, it clearly was not "untimely" or "different relief" for California Portland to contend that if the 1951-52 Case was not followed, the Government's computations are not the only alternative.

Respectfully submitted,

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June, 1968.

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[48] *Id.* at 5, 31.

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

Peter C. Bradford

Nos. 22,397 through 22,398-A

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant

v.

CALIFORNIA PORTLAND CEMENT CO.,

Appellee

CALIFORNIA PORTLAND CEMENT CO.,

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ON APPEALS FROM THE JUDGMENTS OF THE UNITED STATES
DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

REPLY BRIEF FOR THE UNITED STATES AS APPELLANT AND
ANSWERING BRIEF FOR THE UNITED STATES AS CROSS-APPELLEE

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UNITED STATES OF AMERICA,

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ON APPEALS FROM THE JUDGMENTS OF THE UNITED STATES
DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

REPLY BRIEF FOR THE UNITED STATES AS APPELLANT AND [1]
ANSWERING BRIEF FOR THE UNITED STATES AS CROSS-APPELLEE

1/ In accordance with the stipulation filed in this Court on January 18, 1968, the Government filed its opening brief as appellant on or about March 20, 1968; the taxpayer then filed an opening consolidated brief as appellee in the Government's appeals and as cross-appellant in its cross-appeals; and the instant consolidated brief is the Government's reply brief in its own appeals and answering brief in the taxpayer's cross-appeals.

OPINION BELOW

The findings of fact and conclusions of law of the District Court (Nos. 22,397 and 22,397-A, I-R. 119-130; Nos. 22,398 and 22,398-A, I-R. 176-191) are not officially reported.

JURISDICTION

The jurisdictional statement in the Government's opening brief as appellant (pp. 1-3) sets forth all of the jurisdictional facts material to the Government's appeals and, in large part, to the taxpayer's cross-appeals. As taxpayer notes in the jurisdictional statement in its opening consolidated brief (p. 2), the judgments of the District Court became final on July 31, 1967, and taxpayer's notices of appeal were filed on October 6, 1967. (Nos. 22,397 and 22,397-A, I-R. 162, 165; Nos. 22,398 and 22,398-A, I-R. 237, 240.) Taxpayer invokes the jurisdiction of this Court under 28 U.S.C., Section 1291.[2/]

QUESTIONS PRESENTED

The questions presented in the Government's appeals, as set forth in its opening brief (pp. 3-4), are whether the District Court has erroneously interpreted and applied the proportionate profits method in the following respects:

1. In allocating to mining costs the expenses of handling and storing purchased or fully depleted mineral materials (additives) prior to their addition to the kiln feed.

2/ It would appear that the taxpayer's notices of appeal may have been untimely. 28 U.S.C., Section 2107.

2. In excluding from the computation the income from sales of bagged cement, the costs producing such sales, and certain selling expenses.

3. In failing to include in the computation the costs of bags and bagging and the selling expenses as non-mining costs in their entirety.

4. In allocating between mining and non-mining income an inflated gross income figure based on list prices, instead of allocating the actual receipts produced by the so-called discount prices.

The additional questions taxpayer seeks to present on its cross-appeals are:

1. Whether the Government is collaterally estopped from raising the above questions on appeal, by reason of a stipulated District Court judgment as to earlier taxable years of the taxpayer; and

2. Whether if the instant decision of the District Court is not affirmed, taxpayer's loading costs should be treated in accordance with taxpayer's alternative contention below.

STATUTES AND OTHER AUTHORITIES INVOLVED

The statutes and other authorities involved are set forth in Appendix A to the Government's opening brief.

STATEMENT

The material facts, as found by the District Court (Nos. 22,397 and 22,397-A, I-R. 120-127; Nos. 22,398 and 22,398-A, I-R. 176-187), are set forth in the Government's opening brief (pp. 4-10). Insofar as the statement in taxpayer's opening brief is devoted to the findings (pp. 2-3), it is in accord with the Government's statement. Insofar as the taxpayer's statement is devoted to the history and import of prior litigation (pp. 3-5), argumentative matters are involved and accordingly will be dealt with below.

SUMMARY OF ARGUMENT

The merits of the issues raised on the Government's appeals have already been summarized in its opening brief, and no purpose would be served by reiterating that summary here.

The taxpayer's primary contention, on its cross-appeals, is that the Government is foreclosed from a hearing on the merits by the doctrine of collateral estoppel. That contention, rejected by the District Court, was not preserved by the taxpayer's notices of appeal which, in any event, may well have been untimely. Assuming that the contention is properly before this Court, it is patently without merit. Taxpayer invokes the doctrine by reference to litigation involving its earlier taxable years -- more particularly, to District Court rulings entered in 1962 which were (with one exception re-entered in 1965 by stipulation of the parties in order

to conclude the litigation and avoid a third trial. The doctrine does not apply, in the light of the Supreme Court's decision in Commissioner v. Sunnen, 333 U.S. 591, because: (1) The facts were different; (2) the stipulated decision concluding the earlier litigation reserved the Government's right to relitigate the issues; and (3) there have been material intervening changes in the law and legal climate.

The taxpayer's second contention on its cross-appeals is that, if the decision below is not affirmed, this Court should consider its "alternative computation", which was rejected by the District Court. That computation was untimely, being offered by taxpayer some two years after the complaints herein were filed and seeking entirely different relief. Moreover, it is unsupported by any appellate authority or any other final court decision and is contrary to the basic premises and logic of the proportionate profits method.

ARGUMENT

I

THE GOVERNMENT IS NOT BARRED FROM A HEARING ON THE MERITS OF ITS APPEALS BY THE DOCTRINE OF COLLATERAL ESTOPPEL

Taxpayer's primary contention in its opening brief (pp. 8-24) is that the Government is barred from a hearing on the merits of its appeals, under the doctrine of collateral estoppel, by reason of the stipulated findings of fact, conclusions of law and judgment entered on February 16, 1965, in California Portland Cement Co. v. Riddell (S.D. Calif., Central Div., No. 138-58-WM) (18 A.F.T.R. 2d 5424).

The District Court rejected that contention. (Nos. 22,397 and 22,397-A, I-R. 129; Nos. 22,398 and 22,398-A, I-R. 189-190.)[3/] Taxpayer failed to assign the ruling as error in its notices of appeal (Nos. 22,397 and 22,397-A, I-R. 165; Nos. 22,398 and 22,398-A, I-R. 240) which were filed, as noted above, more than sixty days after the District Court's judgments became final. However, the Government does not seek to avoid the issue and assumes hereinafter that it is properly raised.

3/ In its opening brief taxpayer not only ignores the District Court's rejection of its collateral estoppel contention, but asserts (Br. 5, 25 *et seq.*) that the District Court relied upon and followed the very decision on which taxpayer's collateral estoppel argument was and is based. There is nothing in the record to support this assertion; to the contrary, the record shows that the trial judge decided the case on the basis of his own interpretation of certain statutory language. (Nos. 22,397 and 22,397-A, I-R. 117-118; Nos. 22,398 and 22,398-A, I-R. 170-171.)

The cornerstone case on collateral estoppel in tax litigation is, of course, Commissioner v. Sunnen, 333 U.S. 591. Noting therein that the doctrine of collateral estoppel has a much narrower scope than res judicata, the Supreme Court expressed concern lest the doctrine be misapplied to give taxpayers "vested rights" in "obsolete or erroneous" judicial determinations, with resulting "discriminatory distinctions in tax liability, and * * * litigious confusion". (333 U.S., p. 599.) The Court was accordingly at pains to limit the operation of collateral estoppel in tax litigation quite strictly. It envisioned a variety of subtle changes in law, any one of which would lift the bar of estoppel, as where (p. 600) "a judicial declaration intervening between the two proceedings may so change the legal atmosphere as to render the rule of collateral estoppel inapplicable", or where there is "a modification or growth in legal principles as enunciated in intervening decisions of this Court". And the Court cautioned (p. 600) against "neglecting legal modulations by this Court", and against "blind reliance upon the rule of collateral estoppel".

While the examples of intervening decisions given in Sunnen are in terms of the Court's own decisions or decisions of state courts of last resort, Sunnen neither holds nor intimates that these are the only tribunals whose decisions may sufficiently affect the law or legal climate to lift the bar of estoppel. In McCall v. Commissioner, 312 F. 2d 699 (C.A. 4th), the court held that one of

its own prior decisions, together with a decision of the Supreme Court, effected a sufficient "shift in emphasis, if not in basic law, by the Supreme Court and this Court respectively", to lift the bar of estoppel and permit "the important consideration of equality of tax treatment" to prevail. (312 F.,2d p. 706.) More recently, in CBN Corp. v. United States, 364 F. 2d 393, certiorari denied, 386 U.S. 981, the Court of Claims relied upon its own intervening decisions as effecting the necessary change in law or legal climate.

Without regard to changes in the law, the bar of collateral estoppel is averted, of course, if the facts in the later case differ from those involved in the earlier litigation. In this respect, the Supreme Court held in Sunnen that even the most technical factual differences suffice, saying in part (333 U.S., p. 601):

> But if the relevant facts in the two cases are separable, even though they be similar or identical, collateral estoppel does not govern the legal issues which recur in the second case. Thus the second proceeding may involve an instrument or transaction identical with, but in a form separable from, the one dealt with in the first proceeding. In that situation, a court is free in the second proceeding to make an independent examination of the legal matters at issue.

In this connection the Court cited Campana Corp. v. Harrison, 135 F. 2d 334 (C.A. 7th). The court held in that case that the taxpayer had failed to show that the facts before it were precisely the same as those presented in earlier litigation involving earlier taxable years. In so holding, the court stressed

inter alia that (p. 336): "Whether the conditions remain the same as in the former case, no one knows".

In the case at bar it is simply not true, in the first instance, that the facts involved are in all material respects the facts which were presented in the litigation involving taxpayer's earlier years. The two cases differ factually in the following respects, among others:

1. The instant case involves taxpayer's mining and manufacturing operations at two sites, Colton and Mojave. But taxpayer did not begin its operations at Mojave until 1956, and the facts relating to such operations were therefore not involved in the earlier litigation covering the taxable years 1951 and 1952. In this respect, to repeat the above-quoted language from Sunnen, "the relevant facts in the two cases are separable, even though they be similar or identical * * *."

2. Taxpayer concedes (Br. 15-16) that the issue as to handling additives was expressly reserved, without prejudice, in the stipulated decision concluding the earlier litigation. And the District Court did not find (as it did with respect to some issues) that the facts and circumstances relevant to handling additives were the same in both cases. (Nos. 22,398 and 22,398-A, I-R. 185-186.)

3. The evidence of record in the two cases bearing on the discount issue is not the same. To the contrary, as detailed in our

opening brief (pp. 39-42), the instant record shows that -- whatever the nature of the discount may have been in earlier years -- it was a trade discount during the taxable years here involved, reflecting the competitive selling price actually obtained by all major cement producers in taxpayer's market area.4/

In short, the two cases do not present a common and identical factual context, as required by the doctrine of collateral estoppel. Moreover, it should be noted (before turning to substantial intervening changes in the law) that the history and terms of the stipulated decision would, without more, preclude its use as a basis for collateral estoppel. As detailed in taxpayer's brief (pp. 9-12), the earlier litigation had a long and tortuous history involving two trials and two reversals by this Court. And taxpayer is quite correct insofar as it states that (p. 12), on the second remand, the Government wished tc avoid a third trial by stipulating the decision. It would also appear from the colloquy quoted in taxpayer's brief (pp. 12-13, fn. 40) that taxpayer's counsel wanted a decision which would preclude relitigation of all issues except

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4/ In view of this evidence, we submit that it was clear error for the District Court to find (Nos. 22,398 and 22,398-A, I-R. 185-186) that the facts and circumstances relevant to taxpayer's discount practices during the years here involved were in substance identical with the facts and circumstances pertaining to such practices during the earlier taxable years.

the additives issue. On the other hand, taxpayer quotes (Br. 14, fn. 45), with commendable candor, the following statement by Government counsel:

> And although now it doesn't seem, as a matter of law, that we have to be too concerned, nevertheless I wouldn't want it as a matter of record that I have stipulated and that the Government would be so bound. If the collateral estoppel principle is against us, it will be as a matter of law rather than by my agreement.

Whatever the desires and intentions of the respective parties, however, they must yield to the clear and unambiguous provision in the stipulation,as ultimately framed and executed, that (18 A.F.T.R. 2d, p. 5425):

> By agreeing to the entry of the foregoing Findings of Fact and the following Conclusions of Law the defendant has not waived his objection thereto nor does the defendant concede the correctness thereof either for the taxable years in suit or subsequent taxable years. Defendant has stipulated to the entry thereof to avoid another trial for the taxable years involved and so that final Findings of Fact and Conclusions of Law and a final Judgment may be entered without further delay.

We submit that this unqualified language reserved to the Government the right to relitigate the issues with taxpayer for

subsequent taxable years, with or without identity of facts.5/

But the Government's right to relitigate issues involved in the earlier litigation does not rest solely upon the stipulated reservation of that right, or upon factual differences. Wholly apart from those considerations, the doctrine of collateral estoppel is inapplicable here by reason of intervening changes in the law.

The pertinent changes are those occurring after October 8, 1962. On that date the second trial in the earlier litigation concluded in the District Court's entry of comprehensive findings of fact and conclusions of law in California Portland Cement Co. v. Riddell (17 A.F.T.R. 2d 782). The District Court ruled *inter alia* that: (1) Both the income from sales of cement in sacks and the costs producing such sales should be excluded from the proportionate profits computation; and (2) taxpayer's depletable mining income should not be reduced by the amount of its "cash discounts", the costs of loading cement in bulk for shipment to customers, or the costs of purchasing, mining and processing additives. The sole issue on the Government's second appeal was whether the costs of purchasing and mining additives were properly

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5/ Taxpayer is incorrect in its assertion (Br. 8, fn. 20) that the Government prosecuted an appeal from the stipulated decision, and that the appeal was "dismissed". An appeal was never intended, authorized or docketed. A notice of appeal, inadvertently filed, was withdrawn as soon as the error was discovered.

treated by the District Court as includible in taxpayer's mining costs, for the purposes of the proportionate profits computation. This Court reversed on that issue and remanded the case for further proceedings (330 F. 2d 16).

In order to avoid a third trial and bring the seven-year-old litigation to a close, as noted above, a stipulated decision was entered, with a reservation of the Government's right to relitigate, on February 16, 1965. As taxpayer states (Br. 15), and as appears on the face of the stipulation (18 A.F.T.R. 2d 5424), the agreed findings of fact and conclusions of law were those entered on October 8, 1962, with only minor modifications apart from the change required by this Court's reversal on the additives issue. In other words, the application of the proportionate profits method to which the Government agreed in 1965, to avoid a third trial, substantially reflected the law as interpreted by the District Court in its findings and conclusions of October 8, 1962. Quite obviously, then, the question is what changes in the law have occurred since 1962. To determine this it is necessary, at the outset, to review the state of the law in 1962.

In the late 1950's and early 1960's, controversies in the courts over the depletion allowances of integrated miner-manufacturers were focused upon their mining cutoff point -- not upon the detailed application of the proportionate profits method. For a time,

integrated producers of cement and vitrified products successfully contended in various appellate courts that their depletable mining income was their gross income from sales of their finished manufactured products. See, e.g., Dragon Cement Co. v. United States, 244 F. 2d 513 (C.A. 1st, 1957), certiorari denied, 355 U.S. 833, and cases therein cited; the Seventh Circuit's decision in Cannelton Sewer Pipe Co. v. United States, 268 F. 2d 334 (1959); and this Court's first two decisions in the Monolith Portland Cement Co. litigation (Monolith Portland Cement Co. v. United States, 269 F. 2d 629 (1959), and Riddell v. Monolith Portland Cement Co., 301 F. 2d 488 (1962)).

In 1960, however, the Supreme Court reversed the Seventh Circuit's decision in Cannelton, holding (as more fully set forth in the Government's opening brief (pp. 16-17)) that the depletable mining income of an integrated producer of sewer pipe and other vitrified products was its constructive income from its raw minerals, at the point where those minerals were ready for industrial use and consumption. The full sweep of this decision was not immediately apparent. Thus, in its second Monolith decision, entered on March 23, 1962 (301 F. 2d 488), this Court reaffirmed the taxpayer's right to depletion on sales of finished cement, viewing Cannelton as distinguishable in that: (1) It involved different minerals; and (2) there was a commercial market for those minerals, but not for Monolith's limestone. But on January 14, 1963, in Riddell v. Monolith Cement Co., 371 U.S. 537, the Supreme Court

summarily reversed, holding that Cannelton was controlling and that Monolith's depletion base was its constructive income from crushed limestone. 6/

Meantime, the courts had given scant attention, or none, to the proportionate profits method and just how it should be applied. The matter was not of great importance, of course, so long as an integrated producer was authorized by the courts to take depletion on the sales of his manufactured product. There were few computational issues to be raised, and these were of relatively minor importance. For example, on the first Monolith appeal in 1959, the Government's sole assignment of error was that the District Court should have excluded from the taxpayer's depletion base the portion of its gross income attributable to additives -- a view which this Court rejected.

The situation began to change in 1960 with the Cannelton decision. But the scope of Cannelton remained uncertain until the Supreme Court's 1963 decision in Monolith -- and indeed has continued to be litigated by integrated producers seeking depletion on their finished product. See, e.g., United States v. Portland Cement Co. of Utah, 315 F. 2d 169 (C.A. 10th); United States v. Longhorn

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6/ Monolith did not elect the pre-kiln cut-off point made available retroactively to integrated cement manufacturers by the 1960 legislation discussed on pp. 17-18 of the Government's opening brief.

Portland Cement Co., 328 F. 2d 491 (C.A. 5th); United States v. Light Aggregates, Inc., 343 F. 2d 429 (C.A. 8th); Solite Corp. v. United States, 375 F. 2d 684 (C.A. 4th), certiorari denied, 389 U.S. 841. In short, the scope and impact of Cannelton were still much in doubt in 1962, particularly with respect to integrated cement producers.

Nor did the election by cement producers of the pre-kiln cutoff point, under the 1960 legislation, immediately generate detailed judicial consideration of the proportionate profits method in its new context. Indeed, the District Court decision of October 8, 1962, in favor of the instant taxpayer -- our initial point of reference with respect to changes in the law -- was one of the first decisions by any court to deal with the problems of relating the proportionate profits method to the pre-kiln cutoff point. At the end of 1962, none of the appellate courts had considered these problems with respect to electing cement producers, nor had the Court of Claims.

It was not until March 13, 1964, that the Court of Claims entered its decision in Standard Lime and Cement Co. v. United States, 329 F. 2d 939. That decision, later cited with approval by appellate courts, gave extended consideration both to the nature of the proportionate profits method and to its application by reference to the pre-kiln cutoff point of an integrated cement producer.

Generally, the Court of Claims held that: (1) The proportionate profits method is centered on the premise that each dollar of the costs expended to produce and sell the manufactured end product earns the same percentage of the income; (2) costs are allocable to mining only to the extent incurred for the benefit of the mining phase of the producer's operations; and (3) the costs of manufacturing, distributing and marketing finished cement are non-mining costs in their entirety, since no portion of such costs is incurred for the benefit of the mining operations. Specifically, the court held in favor of the Government that the costs of pre-kiln additives, of packing and loading finished cement in bulk and in bags, the costs of bags, and the costs of warehousing were all non-mining costs in their entirety. The court further held that general administrative overhead was allocable between mining and non-mining in a manner in which both the Government and the taxpayer concurred.[7/]

This was the first time a court of national or appellate jurisdiction had reasoned out and adopted a comprehensive set of

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7/ The court also ruled that, on the facts of record, the taxpayer's so-called "cash discount" was a financial expense, and that such expense was allocable between mining and non-mining. In the instant case, as set forth above in our opening brief (pp. 39-42), it is clear on the record that, during the taxable years, taxpayer's so-called discount prices were its actual selling prices, set in competition with the other major producers in the same marketing area, and produced its actual gross income from sales of finished cement.

guidelines for application of the proportionate profits method by reference to the pre-kiln cutoff point of integrated cement producers. The Government subscribed to those guidelines then and does so still. As for the specific computation adopted by the court, this is unclear in some respects; but it is clear that, as to most items of non-mining costs, the court excluded from the computation both the costs and its proportionate part of the profits. As urged in our opening brief, we believe that the simplest and safest proportionate profits computation of depletable mining income will include every dollar of gross sales in the income figure to be allocated between mining and non-mining, and every dollar of the costs producing those sales in the cost fraction. However, the elimination from the computation of an item of non-mining costs together with an accurately-determined proportionate part of the profits, as in Standard Lime, has precisely the same result as if the costs were included in the denominator of the cost fraction and the income figure were left undiminished. Under either approach, an integrated producer's depletion base is only that portion of his gross sales which is produced by his mining costs.

Thereafter, on December 9, 1966, the Third Circuit decided Whitehall Cement Manufacturing Co. v. United States, 369 F. 2d 468. In this decision the court adopted the proportionate profits formula which includes every dollar of costs and every dollar of income,

expressed as: $\frac{\text{mining costs}}{\text{total costs}}$ x gross sales = gross income from mining. Rejecting the taxpayer's contention that costs of loading finished cement for shipment should be allocated between mining and non-mining, the court held that such costs were non-mining in their entirety because they bore no relation to pre-kiln "mining" as defined by statute. In support of this and other rulings, the court cited Standard Lime with approval. Also cited was this Court's decision in Riddell v. Victorville Lime Rock Co., 292 F. 2d 427, in support of the Third Circuit's ruling that costs of bags and bagging, like bulk loading costs, were (p. 474) "properly allocable to the non-mining operations". The court refused to exclude these costs from the computation together with the premium charged for bagged cement, scoring (p. 474) the "erroneous assumption that the packaging costs produced only the additional revenue derived from premiums". The court further held that the costs of additives were non-mining, although incurred prior to the cutoff point, citing this Court's 1964 ruling in Riddell v. California Portland Cement Co., 330 F. 2d 16, that the costs of purchasing and mining additives are not mining costs.

No other appellate court has yet considered specific issues with respect to the constructive mining income of an integrated cement producer, as computed under the proportionate profits method. The Tenth Circuit recognized generally in United States v.

Portland Cement Co. of Utah, 338 F. 2d 798, 802 (1964), that such a computation involves an allocation of profits between mining and non-mining in the proportion which mining costs bear to the total costs of the cement sold. More recently, on May 16, 1967, the Tenth Circuit held in United States v. Portland Cement Co. of Utah, 378 F. 2d 91, certiorari denied, 389 U.S. 975, that the District Court was required to employ the proportionate profits method in computing the taxpayer's depletion base, rather than the substitute materials method proposed by the taxpayer -- which was related to a hypothetical value of the mineral rather than constructive income from mining. 8/ More explicitly than in the earlier appeal in the same litigation, the Tenth Circuit characterized the proportionate profits method as one whereunder (p. 93) --

> the sale price of the product actually sold by the taxpayer (here, the sale price of cement) is allocated to mining according to the ratio that the costs of mining (here, the costs up through primary crushing) bear to the total costs (here, the costs of cement). This method assumes that each cost produces a proportionate part of the profit. 9/

8/ Portland Cement Company of Utah did not elect the pre-kiln cutoff point, and its depletion base is therefore the crushed stone.

9/ Specific applications of the method in determining the mining income of an integrated cement producer who elected the pre-kiln cutoff point are sub judice in the Tenth Circuit in United States v. Ideal Basic Industries, Inc., No. 9,571, on appeal from United States v. Ideal Cement Co., decided by the District Court for the District of Colorado on February 24, 1967 (18 A.F.T.R. 2d 6106). The appeal was argued before the Tenth Circuit on March 12, 1968.

In sum, the state of the law and legal climate is vastly different today from its state in 1962. Decisions of three appellate courts and the Court of Claims, spanning the years from 1964 through 1967, have clarified the nature of the proportionate profits method and have provided both general and specific guidelines for its application in computing the constructive mining income of integrated cement producers. At all points in common, these decisions are in basic accord and, as will appear below, they support or are consonant with the Government's contentions on appeal in the instant litigation. As will also appear, taxpayer errs in its assertion that there are other appellate decisions in point, and that these decisions support the taxpayer's contentions.

Without more, we submit that the Government is not foreclosed on the merits of the instant appeal by the doctrine of collateral estoppel.

II

THE DISTRICT COURT CLEARLY ERRED IN THE RULINGS FROM WHICH THE GOVERNMENT HAS APPEALED

In its opening brief the Government has already discussed in detail the rulings of the District Court from which it has appealed. In this brief our principal concern is with erroneous statements in taxpayer's opening brief with respect to applicable authorities.

A. <u>The costs of handling and storing purchased or fully depleted additives prior to their addition to the kiln feed</u>

In the prior litigation involving the instant taxpayer, this Court held in 1964 (330 F. 2d 16) the taxpayer's costs of purchasing and mining mineral additives were not includible in its mining costs for the purposes of the proportionate profits computation; since the purpose of the computation was to determine taxpayer's constructive income from mining calcium carbonate rock, that income could not be augmented by the costs of mining or, a fortiori, purchasing some other mineral.

The costs of handling and storing the additives separately, prior to their addition to the kiln feed, were not involved on that appeal.[10] But we submit that the rationale of this Court's ruling and the comparable rulings of the Court of Claims in <u>Standard Lime</u> and the Third Circuit in <u>Whitehall</u> require the same result. Costs incurred by taxpayer which are clearly and separately identifiable as relating to iron ore and quartzite are obviously not costs of mining calcium carbonate rock and should not augment taxpayer's depletion allowances thereon. Any other result, as this Court noted, would allow double depletion. As to the additives it mines, taxpayer takes

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10/ Taxpayer concedes (Br. 16) that the Government is not collaterally estopped on this issue.

separate depletion; as to the additives it purchases, depletion is taken by the miner-vendor.

Taxpayer contends (Br. 66) that storing and handling its additives is only "incidental" to mining calcium carbonate rock. We submit that the storage and handling are no more "incidental" than the acquisition of the additives. Taxpayer invokes (Br. 64-65) Rev. Rul. 290, 1953-2 Cum. Bull. 41. But this ruling (revoked by Rev. Rul. 61-17, 1961-1 Cum. Bull. 193) did not involve purchased additives, nor did it hold that costs relating to a mined additive could be utilized to augment depletion allowances on calcium carbonate rock. It held only that mixing of calcium carbonates and shale by the miner thereof <u>before</u> crushing and grinding would be considered incidental to such process -- cautioning that the depletable mining income would have to be computed separately as to each mineral, notwithstanding the mixing. Thus, to the degree that this revoked ruling has any pertinence, it supports the Government's position on handling and storage.

B. <u>The District Court should have included the costs of bags and bagging in the computation, as non-mining costs in their entirety, rather than excluding such costs together with the bag premium</u>

The Third Circuit, in its 1966 decision in <u>Whitehall Cement</u>, held that the costs of bags and bagging, like bulk loading costs, were non-mining expenses in their entirety, citing

Standard Lime and this Court's decision in Riddell v. Victorville Lime Rock Co., supra. The court refused to exclude the costs of bags and bagging from the computation together with the premium charged for bagged cement, rejecting the assumption that there was any correlation between the two and emphasizing, generally, that every dollar of costs and income should go into the proportionate profits computation.

As it must, taxpayer concedes (Br. 21) that Whitehall Cement squarely supports the Government on the costs of bags and bagging. Nor was the Third Circuit making new law in holding that such costs and the costs of bulk loading, alike, are non-mining. Those rulings are in accord with the Court of Claims' rulings in Standard Lime that the costs of bulk loading and bags and bagging are non-mining expenses in their entirety, since no portion of such costs benefits the mining phase of the integrated cement producer's operations. (329 F. 2d, pp. 948-949.) Similarly, this Court's decision in Victorville Lime -- albeit it did not involve an integrated miner-manufacturer or application of the proportionate profits method -- affords general support for the characterization of bagging as a non-mining operation. And the Third Circuit's use of the taxpayer's actual gross sales as the income figure to be allocated, together with its emphasis on including all costs producing the sales in the cost fraction, is the approach more recently adopted by the Tenth

Circuit in United States v. Portland Cement Co. of Utah, 378 F. 2d 91, certiorari denied, 389 U.S. 975 (hereinafter referred to as "the fourth Utah appeal").

Taxpayer attacks Whitehall Cement on a variety of grounds, none of them sound. Taxpayer's assertion (Br. 62) that the Third Circuit was "not advised" as to the starting point in the proportionate profits computation borders on the frivolous; the court quoted and discussed in detail the regulatory definition of the proportionate profits method. Moreover, taxpayer is in error in its assertion that the "first marketable product" is the starting point under the regulation. The starting point is the "representative market * * * price" of the manufactured product, which is equated by the Third and Tenth Circuits with gross sales thereof. The object is to work back from this actual income figure to the taxpayer's constructive income from mining, and not to some hypothetical or constructive value of the mineral, as the Tenth Circuit held in the fourth Utah appeal. Thus, taxpayer is also in error in speaking (Br. 62) of "constructive values" of the kiln feed.

Principally, taxpayer endeavors to show that, on bags and bagging, Whitehall Cement is (Br. 21) "a minority view" and (Br. 62) contrary to "the great weight of authority". But the authorities cited by the taxpayer to support this contention (Br. 32-35) are not in point and hence do not derogate from the clear logic and ruling

in Whitehall Cement. The cases cited by taxpayer do not involve applications of the proportionate profits method to integrated producers; rather they involve determinations, with respect to unintegrated miners, as to their "commercially marketable * * * product" of mining processes. Most of these decisions (including Victorville) took into account the holding in Cannelton that a raw mineral is a commercially marketable product when it is suitable for industrial use and consumption, and can be shipped for such use, whether or not it can be sold at a profit. In Monolith the Supreme Court held that limestone has reached this state when it is crushed. Obviously, then, bagging was not a mining process; the "commercially marketable" product was simply the crude mineral resulting from mining processes, which were then defined by statute as "the ordinary treatment processes normally applied by mine owners or operators". Accordingly, Victorville and the other cases cited by taxpayer held that bagging the crude mineral was a post-mining operation, and the costs thereof could not be reflected in the taxpayer's depletion base.

So far as relevant, these rulings generally support the treatment of the costs of bags and bagging, in the proportionate profits computation, as non-mining costs in their entirety. But they are obviously not directly relevant since they have to do only with a statutory definition of mining processes, no longer in the Code, and a distinction thereunder between mining and post-mining operations.

The proportionate profits method does not call for a distinction in treatment between manufacturing and post-manufacturing costs; the distinction is between mining costs (the numerator of the cost fraction) and total costs (the denominator, which necessarily includes all manufacturing and post-manufacturing costs). The cost fraction controls the allocation of the integrated producer's gross sales between mining and non-mining income. Thus, in the case of a cement producer, every dollar of the costs producing his sales of finished cement must be taken into account on the premise that each dollar of costs earns its proportionate share of the profits.[11/]

11/ It may be noted, in closing the discussion on this point, that taxpayer relies in part (Br. 31, fn. 84) on quoted excerpts from testimony as "evidence" that its "first marketable product" was only cement in bulk. For example, taxpayer quotes Mr. Caldwell's admission (Pltf. Ex. 19, p. 118) of the obvious fact that bagging occurs after the production of bulk cement. However, Mr. Caldwell went on to testify that (p. 119) "the material sold in bags would not otherwise have been sold, except in bags and this probably should be considered as the first commercially marketable product for that material sold in bags". Similarly, Mr. Lintz, as quoted by taxpayer itself, testified that whether cement is sold at the bulk stage or beyond, it is "still cement. The bags have nothing to do with the first marketable product". (Br. 32, fn. 84.)

C. <u>The expenses incurred by taxpayer in selling its manufactured product are non-mining costs in their entirety</u>

In the Government's opening brief, we have already discussed (pp. 36-39) the expenses (largely salesmen's salaries) incurred by the taxpayer in promoting the sales of its manufactured product, finished cement. For the reasons there given, these selling expenses are non-mining in their entirety -- and should be so included in the proportionate profits computation -- since there is no basis in logic, and taxpayer has shown none, for allocating any part of these selling costs to "sales" of kiln feed. Of course, kiln feed is generally not sold commercially; integrated cement producers are deemed to sell it to themselves, under <u>Cannelton.</u> And, as taxpayer concedes (Br. 62), kiln feed is a "fungible product". There is no special quality in a particular producer's kiln feed which would indicate, as a basis for allocation, what the selling expenses of an unintegrated kiln feed producer might be. Accordingly, the selling expenses involved should be included in the denominator of the cost fraction in the proportionate profits computation.

Taxpayer invokes <u>Whitehall Cement</u> as authority for allocating selling expenses between mining and non-mining in the same ratio as general administrative overhead (Br. 21, 51-52, 61), but its reliance is misplaced. Only the District Court so held --

and taxpayer is in error in stating (Br. [illegible]) that the Government did not appeal from that ruling. The Government duly perfected an appeal from that ruling; but the Third Circuit did not reach the issue because its rulings on the taxpayer's appeal were dispositive of the case.

Thus, the issue is one of first impression at the appellate level. We submit that the Government's position is logically sound and is supported by the rationales of Standard Lime, Whitehall Cement and the decision of the Tenth Circuit in the fourth Utah appeal. The Court of Claims did not hold, as taxpayer implies (Br. [illegible]), that selling expenses are for the benefit of, and allocable in part to, the mining phase of a cement producer's operations. So far as relevant, Standard Lime holds only that the expenses of manufacturing and marketing the final product are not for the benefit of the mining operations, in any part, but are non-mining costs in their entirety.

B. The taxpayer's so-called discount prices were, on the record, its competitive selling prices and produced its actual gross sales

As shown in the Government's opening brief (pp. [illegible]), the taxpayer's so-called discount prices -- whatever their original purpose and nature -- are revealed by the record in this litigation as competitive pricing devices which, during the taxable years, yielded the taxpayer's actual gross sales. The taxpayer's answering

arguments (Br. 56-59) are a circular play upon standard definitions of cash discounts and trade discounts. Quite obviously, if a discount is a genuine cash discount -- offered to induce prompt payment, and withdrawn if prompt payment is not forthcoming -- it must be treated as a cash discount. The question is one of fact. In Standard Lime the court found, on the record, that the taxpayer's discount was, in substance as well as in form, a cash discount. The similar finding in the prior litigation involving the instant taxpayer may have been warranted by the facts of record, as to earlier taxable years.

On the record in the instant litigation, the facts simply do not accord with such a finding. As detailed in the Government's opening brief, the so-called cash discount allowed by the taxpayer was precisely the same discount allowed by all of the major producers in taxpayer's marketing area, and was a competitive pricing device. While ostensibly allowed for prompt payment, it was not disallowed as to delinquent customers save in a miniscule percentage of sales. In short, taxpayer's so-called discount prices were its actual selling prices, and produced the gross sales which must be allocated between mining and non-mining income.

III

THE ALTERNATIVE COMPUTATION BELATEDLY PROPOSED BY THE TAXPAYER IN THE DISTRICT COURT IS WITHOUT MERIT

The decision of the District Court in the Ideal Cement Co. case, now pending on appeal in the Tenth Circuit sub nom. Ideal Basic Industries, Inc., as noted above, allocated all post-manufacturing costs of loading, bagging, shipping, warehousing, etc., between mining and non-mining income. (18 A.F.T.R. 2d 6106.) That decision was entered by the District Court (Colo.) on February 24, 1967. The complaints in the instant litigation were filed, as noted in the jurisdictional statements, in 1965. The complaints did not envision the kind of allocations allowed in Ideal Cement; but, since they were so much more favorable to an integrated producer, the instant taxpayer belatedly proposed such allocations as to loading and shipping costs (including bagging) in its so-called "alternative computation". The District Court rejected them. (Nos. 22,397 and 22,397-A, I-R. 117; Nos. 22,398 and 22,398-A, I-R. 170.)

Toward the end of its brief, taxpayer urges (pp. 54-56) that its "alternative computation" be considered in the event that this Court does not affirm outright the decision below. We submit that the contention was untimely below, was and is wholly without merit, and was properly rejected by the District Court. The

taxpayer is not in a position to invoke the District Court decision in Ideal Cement -- even if it were correct, which it is not, and even if it were final, which it is not. In the instant litigation the parties have expressly stipulated that the "processes" applied by the taxpayer to produce cement and prepare it for marketing included storage, sacking and loading for shipment. (Nos. 22,397 and 22,397-A, I-R. 92; Nos. 22,398 and 22,398-A, I-R. 137.) The District Court's decision in Ideal Cement is bottomed upon the proposition that such activities are not such "processes".

A similar allocation advanced by the taxpayer in Whitehall Cement was rejected. Nor is there any basis whatever for the instant taxpayer's suggestion (Br. 56, fn. 142) that Standard Lime, at 329 F. 2d, p. 948, fn. 19, supports an approach even more favorable to the taxpayer. A mere reading of the cited page and footnote shows that this is not so. Whether labeled as "direct non-mining costs" or "non-allocable indirect costs", the result under the proportionate profits method is exactly the same so long as such costs are assumed to produce a proportionate part of the profits. In lieu of the cited footnote 19, we refer this Court to footnote 21 in the Standard Lime opinion, where the court said: "The cost of packing and loading bulk cement and the proportion of the total profits attributable to them must be taken out from the computation in the manner prescribed above".

The taxpayer attempts to draw an analogy between general selling expenses and packing or loading costs. (Br. 55.) However, the taxpayer overlooks the fact that the latter deal with specific quantities of finished cement and by no stretch of the imagination can be allocated back to pre-kiln mining activities. Nor would it be necessary for a non-integrated miner to sack his mineral product. Like selling, packing and loading expenses can be allocated back to mining only if there is some logical and rational basis for making the allocation. In the instant case, the evidence demonstrates that all of such costs relate wholly and entirely to the finished end product rather than to the intermediate mineral product.

Respectfully submitted,

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MAY, 1968.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: 6th day of May, 1968.

Loyal E. Keir

Assistant United States Attorney.